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No. _____

In the

Supreme Court of the United States

October Term, 1997

EARL W. KAVANAU,
Petitioner,

v.

SANTA MONICA RENT CONTROL BOARD,
AN AGENCY OF THE CITY OF SANTA MONICA,
Respondent.

Petition for Writ of Certiorari to the Supreme Court of the State of California

PETITION FOR WRIT OF CERTIORARI

JAMES S. BURLING
*R.S. RADFORD
*COUNSEL OF RECORD
Pacific Legal Foundation
2151 River Plaza Drive,
Suite 305
Sacramento, California 95833
Telephone: (916) 641-8888
Facsimile: (916) 920-3444

Attorneys for Petitioner

113PP

QUESTIONS PRESENTED FOR REVIEW

1. May a state foreclose a remedy of just compensation for a regulatory taking on the grounds that an alternative remedy may be available under the Due Process Clause?

2. Does a citizen whose property is taken by the application of a regulatory scheme forfeit his right to just compensation under the Takings Clause of the Fifth Amendment merely because he acquired the property in question after the enactment of the regulations?

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PETITION FOR WRIT OF CERTIORARI

Petitioner Earl W. Kavanau respectfully prays that a writ of certiorari issue to review the judgment and opinion of the Supreme Court of the State of California, entered in the above-entitled proceeding on August 26, 1997.

OPINIONS BELOW

The decision of the Supreme Court of the State of California is reported at 16 Cal. 4th 761, 941 P.2d 851, 66 Cal. Rptr. 2d 672 (1997), and is reproduced as Appendix (App.) A. The decision of the California Court of Appeal is unreported and is reproduced as Appendix B. The final order of the Superior Court is unreported and is reproduced as Appendix C. Page references herein are to the versions in the appendices.

JURISDICTION

The final decision of the Supreme Court of the State of California was entered on August 26, 1997. The California court considered and decided the question of whether the confiscatory application of a rent control law requires just compensation under the Takings Clause of the Fifth Amendment to the United States Constitution. This petition for writ of certiorari has been timely filed in accordance with Rule 13.1 of the Rules of this Court. This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS AT ISSUE

The Fifth Amendment to the United States Constitution provides in pertinent part, "private property [shall not] be taken for public use, without just compensation."

Section 1 of the Fourteenth Amendment to the United States Constitution provides in pertinent part: "No state shall . . . deprive any person of life, liberty, or property, without due process of law."

STATEMENT OF THE CASE

In a 1993 decision,[1] the California Court of Appeal determined that respondent Santa Monica Rent Control Board's (Rent Board's) imposition of an arbitrary cap on annual rent increases was confiscatory as applied to Earl Kavanau's ten-unit apartment building. This ruling allowed Mr. Kavanau to adjust his rents to a level at which he could begin realizing a fair return on his property. However, the Rent Board's unconstitutional actions had deprived Mr. Kavanau of $113,095 in lost rents over nearly four years before the offending regulations were struck down.[2]

When Mr. Kavanau sued for just compensation for this temporary taking, his complaint was dismissed. The California Supreme Court affirmed, ruling that just compensation was not available since Mr. Kavanau had access to a due process remedy--invalidation of the unconstitutional application of the regulations together with the possibility of future rent adjustments by the Rent Board.

With this decision the California Supreme Court reverts to its historic rule that just compensation is not available in California for temporary regulatory takings. This doctrine,

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[1] *Kavanau v. Santa Monica Rent Control Board*, 19 Cal. App. 4th 730 (1993) (*Kavanau I*). The text of this opinion is reproduced as Appendix E to this petition.

[2] *Kavanau v. Santa Monica Rent Control Board*, No. B087620 (1996) (*Kavanau II*), App. B-3.

previously announced in *Agins v. City of Tiburon*,[3] was expressly overruled by this Court in *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*.[4] In addition to repudiating *First English*, the decision below conflicts with the well-established principle that constitutional claims should be litigated under explicit textual proscriptions (such as the Fifth Amendment's Takings Clause) if applicable, rather than being swept under the more general provisions of the Due Process Clause.

A. The Rent Board Imposes an Arbitrary Limit on Mr. Kavanau's Ability to Recover His Investment in Capital Improvements to His Property

In 1988, Earl Kavanau purchased a small apartment building in Santa Monica, California, that was badly in need of repair. Over the next year Mr. Kavanau incurred expenses in excess of $140,000 for capital improvements and debt service, while his annualized rental income from the property was only $43,444.[5] Mr. Kavanau applied to the Rent Board for permission to increase his rents by an amount sufficient to recover his outlays on capital improvements and debt service and to cover escalating operating costs. The Board determined that Mr. Kavanau was entitled to increases totaling $35,000 per year. However, the Board also imposed an arbitrary limit of 12% on the increases that could be implemented in any 12-month period, even if this policy demonstrably deprived the owner of a fair return on his property.[6]

B. The Court of Appeal Sets Aside the Rent Board's Application of Its Regulations to Mr. Kavanau as Unconstitutionally Confiscatory

Mr. Kavanau petitioned for a writ of administrative mandamus to set aside the Rent Board's decision. The

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[3] 24 Cal. 3d 266, 277 (1979).
[4] 482 U.S. 304, 310-11 (1987).
[5] *Kavanau I*, App. E-2-3.
[6] App. E-3.

California Court of Appeal found that the Board's imposition of an arbitrary 12% limit was "confiscatory" and therefore unconstitutional as applied to Mr. Kavanau.[7] The appellate panel concluded that Mr. Kavanau was entitled to immediate rent increases to secure a fair return on his full investment, without regard to the Rent Board's 12% cap.[8]

This decision remedied the Rent Board's confiscatory actions *prospectively*, *i.e.*, it allowed Mr. Kavanau to adjust his rents to avoid any *further* losses stemming from the Rent Board's unconstitutional application of its annual cap. However, Mr. Kavanau was left bearing the loss of $113,095 in revenues for the period in which the Board's confiscatory policy was enforced.

C. Following Procedures Required by California Law, Mr. Kavanau Seeks--but Is Denied--Just Compensation for the Rent Board's Temporary Regulatory Taking of His Property

Under procedures created by the California Supreme Court, a claim for compensation for an as-applied regulatory taking must be pursued by an inverse condemnation action joined with or subsequent to a petition for administrative mandamus.[9] Having succeeded on his mandamus claim, in 1994 Mr. Kavanau filed suit in inverse condemnation, seeking just compensation for the Rent Board's temporary regulatory taking of his property. This time a divided panel of the Court of Appeal upheld a trial court's dismissal of Mr. Kavanau's complaint, holding that no compensable taking can occur if the owner retains any use of his property.[10] In dissent, Justice Croskey noted that the Court of Appeal's prior decision in *Kavanau I* already established, as a matter of law, that the Rent Board's application of its regulations to Mr. Kavanau violated

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[7] App. E-4-5.
[8] App. E-6.
[9] *Hensler v. City of Glendale*, 8 Cal. 4th 1, 7, 26 (1994).
[10] *Kavanau II*, App. B-9-10.

the Fifth Amendment's Takings Clause. Therefore, the only question properly before the court in *Kavanau II* was the amount of just compensation owed.[11]

D. The California Supreme Court Rules That Just Compensation for a Regulatory Taking Is Not Available if a Due Process Remedy May Exist

The California Supreme Court affirmed on other grounds. In the decision below, the state high court held that Mr. Kavanau was not entitled to just compensation because

> *a remedy for [a] due process violation, if available and adequate, obviates a finding of a taking.*[12]

In this case, the supposedly "adequate" due process remedy consists of Mr. Kavanau's ability to return to the same Rent Board that unconstitutionally deprived him of a fair return on his property eight years ago. He must submit another petition to the Board and either endure another eight years of litigation or (if the rent adjustments should somehow be granted) attempt to recoup from the tenants of his 10 apartments the $113,095 the Board took from him from 1989 through 1993.[13] Clearly, this remedy cannot be described as adequate in the same sense as just compensation--"a full and perfect equivalent for the property taken."[14] On the contrary, the remedy substituted for just compensation by the court below is speculative at best, if not illusory. Nevertheless, it was considered sufficient to eliminate Mr. Kavanau's Fifth Amendment right to just compensation.

The court below underscored its holding by pronouncing the availability of a due process remedy a "benefit" that in itself fulfills the constitutional mandate of just compensation:

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[11] App. B-10-11.

[12] App. A-20 (emphasis added).

[13] App. A-21-25.

[14] *Monongahela Navigation Co. v. United States*, 148 U.S. 312 (1893).

> [T]he Supreme Court has recognized that the benefits a property owner receives in conjunction with a regulation may offset the burdens and thus satisfy the takings clause . . . . Consistent with the reasoning of these cases, . . . *a remedy for the due process violation, if available and adequate, is a valuable benefit that satisfies the takings clause.*[15]

This holding by the court below deprives Earl Kavanau of his Fifth Amendment right to just compensation for the Rent Board's confiscatory application of its arbitrary regulations. More important, it deprives all California property owners of their rights under the Takings Clause. By interpreting the broader and more general protections of the Due Process Clause as a "benefit" that obviates the specific textual guarantee of just compensation, the California court has reverted to its historic doctrine of foreclosing compensation for temporary regulatory takings in California.

REASONS FOR GRANTING THE PETITION

The California Supreme Court has ruled that Earl Kavanau has no compensation remedy under the Fifth Amendment for the temporary regulatory taking of his property if a due process remedy is available. This decision conflicts with the recently enunciated doctrine of the Ninth Circuit Court of Appeals, that a cause of action will not lie for a due process violation if the same facts could give rise to a regulatory takings claim. California citizens who suffer a temporary regulatory taking of their property now face a deadly contradiction: on the same set of facts, the federal courts will not entertain a due process claim, while the state courts will not recognize a just compensation remedy.

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[15] App. A-20 (emphasis added).

The effect of this decision is to return to the rule previously applied in California under *Agins v. City of Tiburon*, that no compensation remedy is available for temporary takings. Under California law, as-applied inverse condemnation claims must be preceded or accompanied by a petition for administrative mandamus seeking to set aside the offending regulatory action as invalid. Yet any application of property regulations that could subsequently be invalidated via a mandamus proceeding would *ipso facto* constitute a violation of due process.[16] By holding that no compensation remedy is available where a due process remedy may be invoked, the California Supreme Court has therefore held that no inverse condemnation claim can be stated for a temporary regulatory taking.

As was the case under *Agins*, this ruling will force California plaintiffs to take their claims for just compensation directly to federal court. Federal jurisdiction for these claims must be recognized because California courts no longer offer a "reasonable, certain and adequate provision" for obtaining just compensation, as required by *Williamson County Regional Planning Commission v. Hamilton Bank of Johnson City*.[17]

Finally, the court below refused to entertain a just compensation remedy in part because Mr. Kavanau acquired his property after rent control was adopted in Santa Monica. According to the California Supreme Court, this gave Mr. Kavanau "constructive knowledge" that the Rent Board might, at any time in the future, apply its regulations in such a way as to take his property without just compensation.[18] This interpretation of the Fifth Amendment's Takings Clause directly conflicts with holdings of the state courts of Florida,

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[16] *See* Cal. Code of Civ. Proc. § 1094.5 (administrative mandamus will issue if respondent proceeded without or in excess of jurisdiction; petitioner did not receive a fair hearing; or there was prejudicial abuse of discretion).

[17] 473 U.S. 172, 194 (1985).

[18] App. A-18.

Massachusetts, and New Jersey, as well as with this Court's teaching in *Lucas v. South Carolina Coastal Council*[19] and *Nollan v. California Coastal Commission*.[20]

Because the doctrine enunciated by the California Supreme Court in the opinion below conflicts with decisions of the courts of three states and with the holdings of the Court of Appeals for the Ninth Circuit, and because the opinion below effectively repudiates this Court's instruction in *First English*, it is imperative that this Court grant the petition for certiorari and reverse the decision below.

I

THIS COURT SHOULD GRANT THE PETITION FOR WRIT OF CERTIORARI TO RESOLVE THE CONFLICT BETWEEN THE CALIFORNIA SUPREME COURT AND THE NINTH CIRCUIT COURT OF APPEALS ON WHETHER THE AVAILABILITY OF A DUE PROCESS REMEDY FORECLOSES A FIFTH AMENDMENT TAKINGS CLAIM

The core doctrinal holding of the decision below is that

> a remedy for the due process violation, if available and adequate, obviates a finding of a taking. . . . [A] remedy for the due process violation, if available and adequate, is a valuable benefit that satisfies the takings clause.[21]

This holding conflicts with this Court's doctrine, expressed in a variety of contexts, that

> [w]here a particular amendment "provides an explicit textual source of constitutional protection" against a particular sort of governmental

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[19] 505 U.S. 1003, 1029 (1994).

[20] 483 U.S. 825, 833 n.2 (1987).

[21] App. A-20-21.

> behavior, "that Amendment, not the more generalized notions of 'substantive due process,' must be the guide for analyzing [a plaintiff's] claims."[22]

The decision below also conflicts with recent decisions of the Ninth Circuit Court of Appeals which hold that the existence of a regulatory takings claim obviates any cause of action for a due process violation on the same facts.

A. In *Armendariz v. Penman*, the Ninth Circuit Established a Rule That the Availability of a Regulatory Taking Claim Obviates a Due Process Cause of Action

In an en banc decision less than two years ago, the United States Court of Appeals for the Ninth Circuit foreclosed due process claims in federal court if a just compensation claim can be stated on the same facts. In *Armendariz v. Penman*,[23] the Court of Appeals held that the protection of the Fourteenth Amendment's Due Process Clause "does not extend to circumstances already addressed by other constitutional provisions."[24]

In *Armendariz*, the plaintiffs alleged a due process violation based on city officials' overzealous enforcement of housing codes and other ordinances. The Court of Appeals concluded that the plaintiffs' due process claim was "preempted" by the more explicit constitutional protections available under the Takings Clause.[25] Relying on this Court's opinions in *Graham v. Connor*[26] and *Albright v. Oliver*,[27] the Ninth Circuit ruled that "[s]ubstantive due process analysis has

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[22] *Albright v. Oliver*, 510 U.S. 266, 273-74 (1994) (Rehnquist, C.J., for plurality) (quoting *Graham v. Connor*, 490 U.S. 386, 395 (1989)).
[23] 75 F.3d 1311 (9th Cir. 1994).
[24] *Id.* at 1325.
[25] *Id.* at 1318.
[26] 490 U.S. 386.
[27] 510 U.S. 266.

no place in contexts already addressed by explicit textual provisions of constitutional protection," such as the Takings Clause.[28]

The *Armendariz* rule, foreclosing due process claims if a just compensation claim can be stated, has quickly become the accepted doctrine of the Ninth Circuit. Late last year *Armendariz* was applied in *Patel v. Penman*[29] to dismiss a due process claim that had been filed concurrently with an action for inverse condemnation. The Ninth Circuit reiterated its *Armendariz* doctrine that a due process claim was "preempted" by the availability of an action for just compensation based on the same facts.[30] Because the plaintiffs "challenge[d] government conduct that is explicitly limited by the Takings Clause of the Fifth Amendment," which "'provides an explicit source of constitutional protection'" against the city's actions, no substantive due process claim could be brought in federal court.[31]

More recently the Ninth Circuit barred a due process cause of action in *Macri v. King County*,[32] a case decided just seven months ago. In *Macri*, plaintiffs alleged violations of the Takings and Due Process Clauses in state court. The action was removed to federal District Court, which stripped the complaint of the due process cause of action under *Armendariz* and remanded the inverse condemnation claim to state court.[33]

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[28] 75 F.3d at 1325-26.

[29] 103 F.3d 868 (9th Cir. 1996).

[30] *Id.* at 875.

[31] *Id.* at 874-75.

[32] 110 F.3d 1496 (9th Cir. 1997).

[33] *Id.* at 1498. This would be the end of the case if it arose in California under *Kavanau*, because the plaintiff's only remedy is for the due process action that was dismissed by the federal court. However, there is a strong argument that a federal court in California would be required to retain jurisdiction over the inverse condemnation cause of action. *See* Section II, *infra*.

The Ninth Circuit affirmed on what was by then the settled law of the circuit:

> when an explicit textual provision of the Constitution protects against the challenged government action, the claim must be analyzed under that specific provision alone and not under the more general guarantee of substantive due process.[34]

Armendariz, *Patel*, and *Macri* evidence a rule of law in the Ninth Circuit wholly contrary to the decision of the California Supreme Court below: when a given set of facts could support either a due process claim or a suit for just compensation under the Takings Clause, only the just compensation claim may be maintained in federal court.[35]

B. The Decision Below Creates an Irreconcilable Conflict Between the California Courts and the Ninth Circuit on a Question of Federal Constitutional Law: On Identical Facts, State Claimants Would Have No Takings Remedy, While Federal Claimants Would Have No Due Process Cause of Action

In the decision below, the California Supreme Court has determined that just compensation for a taking is not available in the courts of that state if an "adequate" due process remedy exists.[36] Thus, because Earl Kavanau could obtain the due process remedy of invalidation accompanied by a remand to the Rent Board, the California courts will not award compensation for the Board's temporary taking of his property.[37]

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[34] *Id.* at 1498-99 (citing *Armendariz*, 75 F.3d at 1325-26).

[35] *Accord*, Thomas E. Roberts, *Takings, Due Process, and Preemption*, 29 Urb. Law. 399, 406-09 (1997) (noting that under this line of decisions "the Takings Clause subsumes substantive due process" in the Ninth Circuit).

[36] App. A-20.

[37] App. A-20-25.

If Mr. Kavanau had filed his complaint in federal District Court, the holding under *Armendariz* would have been precisely the opposite: because the Fifth Amendment guarantees just compensation for a regulatory taking of his property, Mr. Kavanau would not be able to maintain a claim for a due process violation.

The decision below, in conjunction with *Armendariz*, creates a situation in California where federal plaintiffs are deprived of a cause of action for a due process violation, while state plaintiffs are deprived of a remedy for a taking. Virtually any fact situation that would result in a finding of a regulatory taking could also be recharacterized as a due process violation.[38] Thus, for any given injury, the "correct" constitutional cause of action and available relief are dictated entirely by the plaintiff's choice of forum.

This Court should grant certiorari to reconcile the conflict between the California Supreme Court and the Ninth Circuit and restore uniformity in the treatment of federal constitutional claims.

II

IF THIS COURT DOES NOT ACT, THE DECISION BELOW WILL ONCE AGAIN FORCE CALIFORNIA TAKINGS PLAINTIFFS TO TAKE THEIR CLAIMS DIRECTLY TO FEDERAL COURT

The holding of the court below, denying a compensation remedy for temporary regulatory takings, is not new. The same court came to the same conclusion 18 years ago in *Agins v. City of Tiburon*.[39] Because compensation for a temporary regulatory taking was not available in California courts under *Agins*, plaintiffs asserting their rights under the Takings Clause had no

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[38] *See, e.g.*, Thomas E. Roberts, *Takings, Due Process, and Preemption*, 29 Urb. Law. at 407-08 (category of due process claims is broader than regulatory takings claims, but former subsumes latter).

[39] 24 Cal. 3d 266.

option but to take their claims directly to federal court. This Court overruled *Agins* in 1987, but the same misutilization of federal judicial resources will arise anew under the decision below, which effectively reinstates the *Agins* rule.

A. In *Agins v. City of Tiburon*, the California Supreme Court Declared That Just Compensation Is Not Available for Temporary Regulatory Takings in California

In 1979, the California Supreme Court proclaimed in *Agins v. City of Tiburon* that no compensation remedy was available in that state for temporary regulatory takings.[40] Owners whose property was confiscated by excessive regulation were limited to a due process remedy of invalidation unless the government chose to persist in its unconstitutional actions after a taking had been established in court.[41]

Agins was by no means an isolated aberration. Rather, it was the logical culmination of the California Supreme Court's long-standing policy of protecting governmental entities from financial liability for their restrictive land-use policies, regardless of the impact on private citizens.[42] Just compensation, in the view of the California court, was an "inappropriate and undesirable remedy"[43] because "[c]ommunity planners must be permitted the flexibility which their work requires."[44] Being forced to comply with the United States Constitution would supposedly have a "chilling effect"

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[40] *Id.* at 277 ("mandamus or declaratory relief rather than inverse condemnation is the appropriate relief" for a temporary regulatory taking).

[41] *Id.*

[42] *See, e.g., State of California v. Superior Court (Veta)*, 12 Cal. 3d 237 (1974) (declaratory relief or mandamus held to be sole remedy for unconstitutional land-use regulations); *HFH, Ltd. v. Superior Court*, 15 Cal. 3d 508 (1975) (no inverse condemnation remedy for zoning ordinance that does not eliminate substantially all use of land).

[43] *Agins*, 24 Cal. 3d at 275.

[44] *Id.*

that would "intimidate legislative bodies and [] discourage the implementation of strict or innovative planning measures."[45] Finally, the California Supreme Court found it necessary to shield local governments from the Takings Clause because "[i]n enacting a zoning ordinance, the legislative body assesses the desirability of a program on the assumption that compensation will not be required."[46]

In other words, the expectation of California governments that they would be free of liability under the Takings Clause outweighed the expectation of property owners that the authority of the United States Constitution extended to California.

B. Under *Agins*, California Takings Plaintiffs Took Their Fifth Amendment Claims Directly to Federal Court, Since California Did Not Offer the Adequate State Compensation Remedy Specified in *Williamson County Regional Planning Commission v. Hamilton Bank*

In *Williamson County Regional Planning Commission v. Hamilton Bank of Johnson City*,[47] this Court established that regulatory takings claims are not ripe for adjudication in federal court until the plaintiff "seek[s] compensation through the procedures the State has provided for doing so."[48] This requirement, however, was predicated on the availability of a "'reasonable, certain and adequate provision for obtaining compensation'" in state court.[49]

Because no adequate compensation remedy existed in California under *Agins*, property owners seeking their Fifth

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[45] *Id.* at 276.
[46] *Id.*
[47] 473 U.S. 172.
[48] *Id.* at 194.
[49] *Id.* (citations omitted).

Amendment rights were permitted to take their claims directly to federal court, notwithstanding *Williamson County*. The Ninth Circuit was forced to carve out an exception from this Court's ripeness doctrine in recognition of the fact that "California's compensation procedures were inadequate" under *Agins*.[50]

C. This Court Overruled *Agins* in *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*

This Court directly confronted and overruled *Agins* in *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*.[51] Squarely rejecting the California rule that takings claimants could be limited to a due process remedy, this Court decreed, "government action that works a taking of property rights necessarily implicates the 'constitutional obligation to pay just compensation.'"[52] Accordingly, the *Agins* doctrine was overruled as "inconsistent[] with the requirements of the Fifth Amendment."[53]

D. In Response to *First English*, the California Supreme Court Required Regulatory Takings Claimants to First Seek a Due Process Remedy of Invalidation of the Offending Regulations via Mandamus or Declaratory Relief

In response to *First English*, the California Supreme Court created a stringent new procedural rule limiting claims

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[50] *Del Monte Dunes at Monterey, Ltd. v. City of Monterey*, 920 F.2d 1496, 1507 (9th Cir. 1990). *Accord, e.g., Hoehne v. County of San Benito*, 870 F.2d 529, 533 (9th Cir. 1989) (federal court had jurisdiction because under *Agins*, "California law prohibited actions seeking just compensation as a remedy for regulatory takings"); *Sinaloa Lake Owners Association v. City of Simi Valley*, 882 F.2d 1398, 1402 (9th Cir. 1989) (federal court had jurisdiction because under *Agins*, "no action for inverse condemnation based on a regulatory taking could be brought under California law").

[51] 482 U.S. at 310-11.

[52] *Id.* at 315 (quoting *Armstrong v. United States*, 364 U.S. 40, 49 (1960)).

[53] *Id.* at 311.

for regulatory takings. Under the California rule of *Hensler v. City of Glendale*,[54] as-applied regulatory takings claims must proceed by way of administrative mandamus, subject to a statute of limitations of 90 days or less.[55] Only if a takings claimant succeeds in having the offending regulation invalidated via mandamus may he seek compensation via inverse condemnation.[56] What makes this procedural requirement unique is not so much its doctrinal unsoundness[57] as that it effectively requires plaintiffs to pursue a *due process* claim as a prerequisite to seeking just compensation under the Takings Clause.

Under California law, a petition for administrative mandamus seeks to invalidate the application of a regulation or ordinance as an abuse of discretion[58]--the same inquiry that is applied in due process challenges.[59] Moreover, the remedy of invalidation or recision of the offending measure as applied to the plaintiff in question is universally recognized as a due

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[54] 8 Cal. 4th 1.

[55] *Id.* at 21-28.

[56] *Id.* at 13-14.

[57] It has never been the law that only *invalid* statutes or government actions trigger liability under the Takings Clause.

> The *Hensler* opinion was [unclear] on why injured property owners should be forced to seek an *invalidation* remedy--the only relief provided under the cited code sections--when the *legitimacy* of the regulation may be conceded by the owner from the outset. . . . Until now, it had not been suggested that a writ of administrative mandamus is required to remedy *permissible* governmental actions.

Sharon L. Browne, *Administrative Mandamus as a Prerequisite to Inverse Condemnation: "Healing" California's Confused Takings Law*, 22 Pepperdine L. Rev. 99, 125 (1994).

[58] Cal. Code of Civ. Proc. § 1094.5(b).

[59] *See, e.g., Kensington University v. Council for Private Postsecondary and Vocational Education*, 54 Cal. App. 4th 27, 30 (1997).

process remedy.[60] Thus, in effect, the initial response of the California Supreme Court to *First English* was to establish that regulatory takings plaintiffs must pursue a due process action before compensation under the Takings Clause will be considered. Compensation via inverse condemnation was no longer foreclosed, as under *Agins*, but was held out as a follow-on possibility for plaintiffs who succeeded in their claim for a due process remedy of invalidation.

E. By Ruling That a Due Process Remedy Obviates a Claim for Just Compensation, the Decision Below Reverts to Agins' Rule That No Compensation Remedy Is Available for Temporary Regulatory Takings in California

In the case at bar, Earl Kavanau complied to the letter with California's rigorous procedural demands. His administrative mandamus petition was filed within 90 days of the Rent Board's confiscatory actions and--most remarkable of all--Mr. Kavanau obtained a judgment from a California appeals court in his favor, finding the Rent Board's regulations to be unconstitutionally "confiscatory" as applied to him.[61] But at that point the door was slammed.

Faced with the prospect of actually subjecting an entity of California government to the discipline of the Takings Clause, the court below determined that a due process remedy was not only a *prerequisite to*, but a *substitute for* just compensation.[62] Because Mr. Kavanau could return to the very Rent Board that had willfully deprived him of a fair return on his property and go through the petitioning process anew, the court below ruled that the availability of these procedures "obviates" a claim for just compensation.[63]

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[60] *See, e.g., Williamson County*, 473 U.S. at 197 ("The remedy for a regulation that goes too far, ***under the due process theory***, is not 'just compensation,' but invalidation of the regulation . . . .") (emphasis added).

[61] *Kavanau I*, App. E-4-6.

[62] App. A-20-21.

[63] *Id.*

By upholding the dismissal of Mr. Kavanau's inverse condemnation complaint, the California Supreme Court effectively repudiated this Court's instruction in *First English* that

> a landowner is entitled to bring an action in inverse condemnation as a result of "the self-executing character of the constitutional provision with respect to compensation."[64]

Because every takings claimant is required, under California's procedural scheme, to obtain a due process remedy as a prerequisite to pursuing inverse condemnation, the decision below forecloses just compensation in nearly every case. The only exceptions will be where the government persists in the application of its regulations after a court pronounced them to be invalid.

But this was precisely the doctrine of the California Supreme Court under *Agins v. City of Tiburon!* Ten years after this Court corrected the court below in *First English*, the *Agins* rule has been resurrected: just compensation is (in theory) available in California for a *permanent* regulatory taking, but never for a temporary one.

Unless this Court acts, the conflict identified in the preceding section will be "resolved" by forcing all California takings plaintiffs into federal court. As was the case under *Agins*, federal jurisdiction will be invoked by regulatory takings claimants because, under *Kavanau*, California courts no longer afford a "reasonable, certain and adequate"[65] provision for obtaining just compensation. This undesirable outcome can be avoided only by granting the petition for certiorari and reversing the court below.

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[64] *First English*, 482 U.S. at 315 (citations omitted).

[65] *Williamson County*, 473 U.S. at 194.

III

THIS COURT SHOULD GRANT THE PETITION TO RESOLVE THE CONFLICT AMONG THE STATE AND FEDERAL COURTS AS TO WHETHER AN OWNER WHO ACQUIRES REGULATED PROPERTY FORFEITS HIS FIFTH AMENDMENT RIGHTS IF THOSE REGULATIONS ARE SUBSEQUENTLY APPLIED TO CONFISCATE HIS PROPERTY

Even though *Kavanau I* established, as law of the case, that the Rent Board's application of its regulations was unconstitutionally confiscatory as applied to Mr. Kavanau, the court below found that just compensation was not available under the Fifth Amendment. This ruling was based in part on the fact that Santa Monica's rent control law had been enacted prior to Mr. Kavanau's purchase of his property. When the Rent Board subsequently applied this law unconstitutionally, Mr. Kavanau was stripped of his rights under the Fifth Amendment because he supposedly "had constructive knowledge" that the Rent Board might violate the United States Constitution at some future time.[66]

California thus joins New York State in extinguishing the Fifth Amendment rights of citizens who purchase regulated property. The New York Court of Appeals has recently held that the enactment of property regulations comprises an immediate encumbrance on the title of subsequent purchasers.[67] The confiscatory application of such regulations therefore "does not constitute a governmental taking of any property interest owned" by citizens who acquire title after the

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[66] App. A-18.

[67] *See Anello v. Zoning Board of Appeals*, 89 N.Y.2d 535 (1997); *Gazza v. New York State Department of Environmental Conservation*, 89 N.Y.2d 603 (1997); *Kim v. City of New York*, 90 N.Y.2d 1(1997); *Basile v. Town of Southhampton*, 89 N.Y.2d 974 (1997).

regulatory scheme is in place.[68] This reasoning was mirrored by the court below, which found that the Rent Board's unconstitutional confiscation of Mr. Kavanau's property comprised only a "minor" interference with his expectations, since the statute supposedly authorizing the Board's unconstitutional actions predated Mr. Kavanau's acquisition of the property.[69]

A. The Decision Below Conflicts with the State Courts of Florida, Massachusetts, and New Jersey on the Important Federal Question of Whether Fifth Amendment Rights Are Extinguished Merely Because a Citizen Acquires Real Property After Land Use Regulations Have Been Adopted

The Florida District Court of Appeal rejected the doctrine of the decision below in *Vatalaro v. Department of Environmental Regulation*.[70] There, the Florida court held that the denial of a permit constituted a regulatory taking of property even though the denial was based on a regulation that existed before the owner acquired her land. This ruling, that a violation of the Takings Clause requires just compensation even if the taking is "authorized" by preexisting legislation, directly conflicts with the California court's ruling that Mr. Kavanau was not entitled to compensation because he had "constructive knowledge" that the Rent Board might violate his constitutional rights.

Similarly, in *Lopes v. City of Peabody*,[71] the Supreme Judicial Court of Massachusetts held that a property owner has a right to compensation for a taking arising from the application

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[68] *Anello v. Zoning Board of Appeals*, 89 N.Y.2d at 540.

[69] App. A-18.

[70] 601 So. 2d 1223, 1229 (5th Dist. Fla.), *review denied*, 613 So. 2d 3 (Fla. 1992).

[71] 32 Mass. App. Ct. 1124, 595 N.E.2d 812, *review denied*, 413 Mass. 1105, 600 N.E.2d 171 (1992), *cert. granted and judgment vacated*, 507 U.S. 981 (1993), *on remand*, 417 Mass. 299, 629 N.E.2d 1312 (1994).

of a land-use restriction predating the owner's acquisition of his land.

The *Lopes* plaintiff acquired a lot that was subject to a wetlands ordinance enacted six years earlier.[72] When the City denied a permit to build a residence on the regulated land, the Massachusetts Supreme Judicial Court ruled that Mr. Lopes had a right to pursue an inverse condemnation remedy even though his property was "subject to the restriction at the time of his purchase."[73]

Finally, the decision below conflicts with the state courts of New Jersey. In *Moroney v. Mayor and Council of the Borough of Old Tappan*,[74] the New Jersey appellate court upheld a finding that a landowner was entitled to pursue a takings remedy for the denial of a building permit based on preexisting zoning regulations. Noting that someone who owned the property prior to the adoption of restrictive zoning could have pursued a takings claim, the New Jersey court ruled that property owners "stand in the shoes of their predecessors in title" to challenge the application of such measures.[75]

In the case at bar, Earl Kavanau was deprived of his right to just compensation under the Takings Clause in part because he acquired title to his property after rent control was imposed in Santa Monica. This ruling directly conflicts with *Vatalaro*, *Lopes*, and *Moroney*, and deepens the conflict among the states on this essential issue of federal constitutional law. This Court should grant certiorari to restore uniformity among

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[72] 417 Mass. at 303, 629 N.E. 2d at 1314-15.

[73] *Id. But see Leonard v. Town of Brimfield*, 423 Mass. 152, 155, 666 N.E.2d 1300, 1303 (1996) (limiting the extent to which a landowner can claim takings damages for a preexisting regulation).

[74] 268 N.J. Super. 458, 633 A.2d 1045 (1993), *cert. denied*, 136 N.J. 295, 642 A.2d 1004 (1994).

[75] 633 A.2d at 1047.

the state courts of California, New York, Florida, Massachusetts, and New Jersey.

B. The Decision Below Would Strip Citizens of Their Right to Just Compensation Whenever Regulated Property Changes Hands, Contrary to This Court's Doctrine in *Lucas* and *Nollan*

In *Lucas v. South Carolina Coastal Council*, this Court held that limitations on the use of property that would otherwise violate the Takings Clause may remain uncompensated only if the limitations "inhere in the title itself, in the restrictions that background principles of the State's law of property and nuisance already place upon land ownership."[76] If these "background principles" are expanded to include any and all restrictive legislation enacted prior to a given owner's purchase of his property, the protections of the Takings Clause would quickly evaporate.

As Justice Holmes observed long ago, when the "seemingly absolute" requirement of just compensation

> is found to be qualified by the police power, the natural tendency of human nature is to extend the qualification more and more until at last private property disappears.[77]

The decision below provides a clear illustration of Justice Holmes' foresight. If the mere enactment of rent control insulates the City of Santa Monica from any claims for compensation based on the unconstitutional application of that law to subsequent buyers of rental property, an ever-growing segment of the population will be deprived of their federal constitutional rights.

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[76] 505 U.S. at 1029.

[77] *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922).

This Court expressly held in *Nollan v. California Coastal Commission* that private ownership rights are not altered merely because property is acquired after a restrictive land-use policy is implemented.[78] The full "bundle" of ownership rights runs with the land: "Prior owners must be understood to have transferred their full property rights" when they convey title.[79] In contrast, under the reasoning employed by the court below, the prior owner's right to pursue a compensation remedy for a taking is extinguished when land changes ownership following the enactment of potentially restrictive regulations.

CONCLUSION

For the reasons stated above the petition for writ of certiorari should be GRANTED.

DATED: November, 1997.

Respectfully submitted,

JAMES S. BURLING
*R.S. RADFORD
*COUNSEL OF RECORD
Pacific Legal Foundation
2151 River Plaza Drive,
Suite 305
Sacramento, California 95833
Telephone: (916) 641-8888
Facsimile: (916) 920-3444

Attorneys for Petitioners

[78] 483 U.S. at 833 n.2.
[79] *Id.*

APPENDIX

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IN THE SUPREME COURT OF CALIFORNIA

Earl W. KAVANAU, Plaintiff and Appellant, v. SANTA MONICA RENT CONTROL BOARD, Defendant and Respondent.	No. S051847 Ct. App. 2/3 B087620 Los Angeles County Super. Ct. No. BC 103933

***675** Earl W. Kavanau, in pro. per., Plaintiff and Appellant.

James S. Burling, R.S. Radford, Sacramento, Paul C. Mileck, Berkeley, Sherman L. Stacey, Santa Monica, Kimball & Weiner and George Kimball, Los Angeles, Amici Curiae on behalf of Plaintiff and Appellant.

Anthony A. Trendacosta, Ralph H. Goldsen, Doris Ganga, Karl M. Manheim, Hedges & Caldwell, David Pettit and Joan Mack, Los Angeles, for Defendant and Respondent.

Louise H. Renne, City Attorney, San Francisco, Andrew W. Schwartz, Deputy City Attorney, Richards, Watson & Gershon and Rochelle Browne, Los Angeles, Amici Curiae on behalf of Defendant and Respondent.

CHIN, Justice.

In this case, we consider the inverse condemnation claim of Earl W. Kavanau, a property owner who prevailed in a prior action against the Santa Monica Rent Control Board (Rent Board) on the ground that the rent control regulations of the City of Santa Monica (the City) violated his right to due process of law. The Court of Appeal affirmed the trial court's dismissal order, rejecting Kavanau's inverse condemnation claim because he had not lost "all use of his property." We disagree that a property owner must lose all use of his property in order to have a viable inverse condemnation claim. Nevertheless, we conclude Kavanau is not entitled to maintain an

inverse condemnation action, because he may obtain a full and adequate remedy for any interim loss flowing from the due process violation through an adjustment of future rents under the rent regulation process. Accordingly, we affirm the judgment of the Court of Appeal.

FACTUAL ALLEGATIONS AND PROCEDURAL BACKGROUND

Kavanau's complaint alleges as follows. In 1988, he purchased a 10-unit apartment building in the City. At that time, the building was already subject to the City's rent control law, which limited rent increases to 12 percent per year regardless of increases in landlord expenses. Between November 1, 1988, and October 31, 1989, Kavanau collected rents totaling $43,444 and spent $33,565 operating and maintaining the property, $82,934 improving the property, and $44,000 servicing debt on the property. On November 30, 1989, Kavanau applied to defendant Rent Board for rent increases on nine of the ten units in his building. The Rent Board's hearing examiner determined Kavanau was entitled to rent increases totaling approximately $35,000 per year, but required Kavanau to impose these increases over the course of eight years so as not to exceed the 12 percent limit in any one year. The hearing examiner approved rent increases for the first year totaling $5,184.

Kavanau appealed the hearing examiner's decision to the Rent Board, which upheld the decision. Kavanau then petitioned the superior court for a writ of administrative mandate, which the court denied. Kavanau appealed, and the Court of Appeal reversed. *676 (Kavanau v. Santa Monica Rent Control Bd. (1993) 19 Cal.App.4th 730, 736, 23 Cal.Rptr.2d 724 (Kavanau I).)

In Kavanau I, the Court of Appeal concluded that the 12 percent limit on rent increases deprived Kavanau of "a just and reasonable return" and therefore was unconstitutional. (Kavanau I, supra, 19 Cal.App.4th at p. 736 & fn. 7, 23 Cal.Rptr.2d 724.) The Court of Appeal directed the superior court to issue a writ of mandate prohibiting application of the 12 percent limit to his rent increase petition. (Id. at pp. 736- 737, 23 Cal.Rptr.2d 724.) We denied the Rent Board's petition for review. The Rent Board complied with the superior court's mandate.

Kavanau then filed the complaint in this case, seeking damages for temporary application of the 12 percent limit. In his first cause of action, he alleges he "has suffered a 'taking' and 'damaging' of his property rights" within the meaning of article I, section 19 of the California Constitution and the Fifth Amendment of the United States Constitution. He seeks "just compensation" in the form of lost rental income and interest. In his second cause of action, Kavanau alleges a violation of his right to due process of law and seeks damages, including emotional distress damages, under 42 United States Code section 1983 (section 1983).

The Rent Board demurred to Kavanau's complaint, and the superior court sustained the demurrer without leave to amend. Kavanau appealed, and the Court of Appeal affirmed. The Court of Appeal noted that Kavanau had abandoned his cause of action under section 1983. As for the cause of action alleging a taking of his property requiring just compensation under the state and federal Constitutions, the Court of Appeal rejected Kavanau's claim because he never lost "all use of his property." For example, he continued to receive rents and enjoy tax benefits, and he could borrow against the property, hold it for investment, convert it to condominiums, or sell it. One justice dissented, stressing that Kavanau I had already decided the Rent Board had applied its regulations in an unconstitutional manner. Because Kavanau lost substantial rental income as a result of this constitutional breach, the dissenting justice argued Kavanau had suffered a taking of his property and should receive just compensation. We granted review in order to consider whether a taking occurred and what, if any, right to just compensation Kavanau might have.

THE CITY'S RENT CONTROL LAW

[1][2][3] Rent control laws must be "reasonably calculated to ... provide landlords with a just and reasonable return on their property." (Birkenfeld v. City of Berkeley (1976) 17 Cal.3d 129, 165, 130 Cal.Rptr. 465, 550 P.2d 1001 (Birkenfeld).) In order to satisfy this standard, rent control laws incorporate any of a variety of formulas for calculating rent ceilings. (See Baar, Guidelines for Drafting Rent Control Laws: Lessons of a Decade (1983) 35 Rutgers L. Rev. 723, 781-817 (Guidelines) [discussing various rent control formulas].) "Rent control agencies are not obliged by either the state

or federal Constitution to fix rents by application of any particular method or formula." (Carson Mobilehome Park Owners Assn. v. City of Carson (1983) 35 Cal.3d 184, 191, 197 Cal. Rptr. 284, 672 P.2d 1297 (Carson).) Rather, "selection of an administrative standard by which to set rent ceilings is a task for local governments ... and not the courts." (Fisher v. City of Berkeley (1984) 37 Cal. 3d 644, 681, 209 Cal.Rptr. 682, 693 P.2d 261 (Fisher); cf. Power Comm'n v. Natural Gas Pipeline Co. of America (1942) 315 U.S. 575, 586, 62 S.Ct. 736, 743, 86 L.Ed. 1037 (Pipeline Co.) ["The Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas."].)

The City uses a "maintenance of net operating income" formula for calculating rent ceilings. A typical maintenance of net operating income formula presumes the landlord's net operating income at the time rent control began provided a just and reasonable return. In order to maintain this net operating income at a constant level, the law permits rent increases that will enable the landlord to recoup increases in ongoing operating expenses. (See Guidelines, supra, 35 Rutgers L. Rev. at pp. 809-817.) The landlord may also amortize the costs of capital improvements over the useful life of those improvements *677 and pass those costs through to tenants. (See id. at pp. 817-826.) Of course, if the law holds net operating income constant, inflation will erode the real value of that income. Thus, many maintenance of net operating income formulas permit a periodic inflation adjustment. (See Fisher, supra, 37 Cal.3d at p. 683, 209 Cal.Rptr. 682, 693 P.2d 261; cf. Cotati Alliance for Better Housing v. City of Cotati (1983) 148 Cal.App.3d 280, 289, 195 Cal.Rptr. 825 (Cotati).)

The City's rent control law conforms generally to this model. An April 10, 1979, amendment to the City Charter (Charter) created the Rent Board and empowered it "to regulate rentals ... so that rents will not be increased unreasonably and so that landlords will receive no more than a fair return." (Charter, § 1800.) Pursuant to this charter amendment (Charter, § 1803(g)), the Rent Board adopted comprehensive regulations (Rent Board Regulations).

The Charter amendment rolled back most residential rents in the City to their level on April 10, 1978. (Charter, § 1804(b); Rent Bd. Regs., regs. Nos. 7000-7001.) This rollback established the base rent

for individual rental units in the City. (Charter, § 1804(b).) To accommodate subsequent changes in landlord expenses, the Rent Board has since authorized various general rent adjustments and surcharges. (Charter, § 1805(a), (b); Rent Bd. Regs., regs. Nos. 3000- 3106.) In addition, a landlord can petition for an individual rent adjustment in lieu of applicable general adjustments (Charter, § 1805(c); Rent Bd. Regs., regs. Nos. 4100-4114), in which case a hearing examiner receives evidence and prepares a decision, including findings of fact and law (Charter, § 1805(d); Rent Bd. Regs., regs. Nos. 4007-4020). Either party may appeal the hearing examiner's decision to the Rent Board. (Charter, § 1805(d)(10); Rent Bd. Regs., reg. No. 4021.)

The Rent Board Regulations define net operating income as gross income less operating expenses. (Rent Bd. Regs., regs. Nos. 4101(a), 4104.) The Rent Board Regulations also establish a presumption that the net operating income during the 1978 calendar year provided a landlord with a fair return. (Rent Bd. Regs., reg. No. 4102.) A landlord can rebut this presumption by showing that operating expenses during 1978 were unusually high (Rent Bd. Regs., reg. No. 4103A) or that base rent was unusually low (Rent Bd. Regs., reg. No. 4103B). A landlord is entitled not only to maintain 1978 net operating income (Rent Bd. Regs., reg. No. 4102), but also to petition for rent increases that will increase net operating income at a rate equal to 40 percent of any increase in the consumer price index (Rent Bd. Regs., reg. No. 4106).

To establish an erosion of net operating income, and therefore entitlement to a rent increase, a landlord may present evidence of an increase in operating expenses. Under the Rent Board Regulations, operating expenses include capital improvement costs (Rent Bd. Regs., reg. No. 4101(c)(1) (viii)), but the landlord must amortize these costs over their useful life in accordance with an amortization schedule (Rent Bd. Regs., reg. No. 4041(a)-(c)).

At the time Kavanau improved his property, a landlord who had no financing costs could include an imputed interest cost as part of his capital improvement costs. (Former Rent Bd. Regs., reg. No. 4041(d).) Also at that time, a capital improvement rent increase lapsed once the amortization period ended (i.e., once the landlord had recouped all the costs associated with the improvement). (Former

Rent Bd. Regs., reg. No. 4041(e).) Under current Rent Board Regulations, a capital improvement rent increase is permanent, allowing the landlord eventually to recoup more than his total cost. (Rent Bd. Regs., reg. No. 4041(c).)

The Rent Board Regulations protect tenants from sudden, large rent increases by delaying rent increases that would otherwise be permissible. At the time the Court of Appeal decided Kavanau I, a landlord could not increase rent more than 12 percent in any 12-month period, except in "extraordinary circumstances" such as an earthquake. (Former Rent Bd. Regs., reg. No. 4107(a), (f).) This 12 percent limit is central to the dispute in this case. Current Rent Board Regulations impose this limit only in the case ***678** of tenant hardship. (Rent Bd. Regs., reg. No. 4107(a).)

DISCUSSION

Two independent constitutional protections are at issue in this case. The due process clauses of the state and federal Constitutions guarantee property owners "due process of law" when the state "deprive[s] [them] of ... property." (Cal. Const., art. I, §§ 7, 15; U.S. Const., 14th Amend., § 1.) On the other hand, the takings clauses of the state and federal Constitutions guarantee property owners "just compensation" when their property is "taken for public use." (Cal. Const., art. I, § 19; U.S. Const., 5th Amend.) These distinct constitutional protections limit the legislative power of government in different but related ways. The due process protection focuses on the government's means and purpose: whether the government's method rationally furthers legitimate ends. The takings protection focuses on the impact of the government's action: whether the government has in effect appropriated private property for its own use, rather than merely regulating a private use of the property. This conceptual distinction, however, blurs somewhat in cases applying the due process and takings clauses to price regulations, including rent control. In that context, courts sometimes employ overlapping terminology and standards, treating the two clauses as a single constitutional protection of private property rights.

Deprivation of Property Without Due Process of Law

[4][5] The state and federal Constitutions prohibit government from depriving a person of property without due process of law.

(Cal. Const., art. I, §§ 7, 15; U.S. Const., 14th Amend., § 1.) These provisions guarantee appropriate procedural protections (see, e.g., Goldberg v. Kelly (1970) 397 U.S. 254, 90 S.Ct. 1011, 25 L.Ed.2d 287) and also place some substantive limitations on legislative measures (see, e.g., Washington v. Glucksberg (1997) --- U.S. ----, 117 S.Ct. 2258, 138 L.Ed.2d 772; U.S. v. Carolene Products Co. (1938) 304 U.S. 144, 58 S.Ct. 778, 82 L. Ed. 1234; Nebbia v. New York (1934) 291 U.S. 502, 54 S.Ct. 505, 78 L.Ed. 940 (Nebbia)). The latter guaranty--sometimes described as substantive due process--prevents government from enacting legislation that is "arbitrary" or "discriminatory" or lacks "a reasonable relation to a proper legislative purpose." (Nebbia, supra, 291 U.S. at p. 537, 54 S.Ct. at p. 516.)

[6][7][8][9][10][11] In the context of price control, which includes rent control, courts generally find that a regulation bears "a reasonable relation to a proper legislative purpose" so long as the law does not deprive investors a "fair return" and thereby become "confiscatory." (Pipeline Co., supra, 315 U.S. at pp. 584, 585, 62 S.Ct. at pp. 742-743; see also Power Comm'n v. Hope Natural Gas Co. (1944) 320 U.S. 591, 602-603, 64 S.Ct. 281, 287-288, 88 L.Ed. 333 (Hope Gas); 20th Century Ins. Co. v. Garamendi (1994) 8 Cal.4th 216, 292-296, 32 Cal.Rptr.2d 807, 878 P.2d 566 (20th Century); Calfarm Ins. Co. v. Deukmejian (1989) 48 Cal.3d 805, 816, 258 Cal.Rptr. 161, 771 P.2d 1247 (Calfarm); Guidelines, supra, 35 Rutgers L.Rev. at pp. 781- 817.) Determining prices that will provide a fair return "involves a balancing of the investor and the consumer interests." (Hope Gas, supra, 320 U.S. at p. 603, 64 S.Ct. at p. 288.) "It is the product of expert judgment which carries a presumption of validity." (Id. at p. 602, 64 S.Ct. at pp. 287- 288.) A reviewing court focuses on whether the regulatory agency took relevant investor interests into account. (Permian Basin Area Rate Cases (1968) 390 U.S. 747, 770, 88 S.Ct. 1344, 1361-1362, 20 L. Ed.2d 312 (Permian Basin); Pipeline Co., supra, 315 U.S. at p. 586, 62 S.Ct. at p. 743.) One of these investor interests is a "return ... commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to ... attract capital." (Hope Gas, supra, 320 U.S. at p. 603, 64 S.Ct. at p. 288.) Though due process protections generally focus on method, not result, in the context of price regulation "it is the

result reached not the method employed which is controlling. [Citations.] It is not theory but the impact of the [price regulation] which counts." (Id. at p. 602, 64 S.Ct. at pp. 287- 288.) In sum, when considering *679 whether a price regulation violates due process, a "court must determine whether the [regulation] may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection for the relevant public interests, both existing and foreseeable." (Permian Basin, supra, 390 U.S. at p. 792, 88 S.Ct. at p. 1373.)

We applied these due process standards to rent control laws in Fisher, supra, 37 Cal.3d 644, 209 Cal. Rptr. 682, 693 P.2d 261, Carson, supra, 35 Cal.3d 184, 197 Cal.Rptr. 284, 672 P.2d 1297, and Birkenfeld, supra, 17 Cal.3d 129, 130 Cal.Rptr. 465, 550 P.2d 1001. Though the state and federal Constitutions do not mandate a particular administrative formula for measuring fair return (Fisher, supra, 37 Cal.3d at p. 681, 209 Cal.Rptr. 682, 693 P.2d 261), we did note certain characteristics that would weigh in favor of a finding of constitutionality. For example, due to the effects of inflation, the law "may not indefinitely freeze the dollar amount of ... profits without eventually causing confiscatory results." (Id. at p. 683, 209 Cal.Rptr. 682, 693 P.2d 261, original italics.) In addition, when a rent control law establishes a "base rent" by reference to rents on a specified date, the law should permit adjustments of that base rent for those rental units that had artificially low rents at that time. (Birkenfeld, supra, 17 Cal.3d at p. 168, 130 Cal.Rptr. 465, 550 P.2d 1001.) Similarly, the law should permit individualized rent adjustments in appropriate cases even if base rent was not artificially low (Fisher, supra, 37 Cal. 3d at pp. 689-690, 209 Cal.Rptr. 682, 693 P.2d 261), and the procedural mechanism by which landlords may obtain any of these adjustments must not be prohibitively burdensome (Birkenfeld, supra, 17 Cal.3d at pp. 169-171, 130 Cal.Rptr. 465, 550 P.2d 1001; see also Fisher, supra, 37 Cal.3d at p. 690, 209 Cal.Rptr. 682, 693 P.2d 261). Among other things, this process may not entail "a substantially greater incidence and degree of delay than is practically necessary." (Birkenfeld, supra, 17 Cal.3d at p. 169, 130 Cal.Rptr. 465, 550 P.2d 1001; see also Fisher, supra, 37 Cal.3d at p. 687, 209 Cal.Rptr. 682, 693 P.2d 261.) In this regard, we recommended that the law permit "general rental adjustments for all or any class of rental units based

on generally applicable factors." (Birkenfeld, supra, 17 Cal.3d at p. 171, 130 Cal.Rptr. 465, 550 P.2d 1001; see also Fisher, supra, 37 Cal.3d at p. 687, 209 Cal.Rptr. 682, 693 P.2d 261; but see Carson, supra, 35 Cal.3d at p. 194, 197 Cal.Rptr. 284, 672 P.2d 1297.) We also indicated rent control laws should (1) allow landlords to petition for rent adjustments without having to prove building code compliance, (2) allow the governing agency to consolidate petitions for rental units in the same building, and (3) allow the governing agency to delegate hearings on petitions to hearing officers. (Birkenfeld, supra, 17 Cal.3d at pp. 170-171, 130 Cal.Rptr. 465, 550 P.2d 1001; see also Fisher, supra, 37 Cal.3d at pp. 690-691, 209 Cal.Rptr. 682, 693 P.2d 261.) All these characteristics would serve to reduce delay and make the petition process less burdensome to landlords, but we did not hold the state or federal Constitution required any of them per se.

[12] Of course, the fair return principle is not limited to the property as it was when the landlord purchased it. A landlord is also entitled to a fair return on necessary capital improvements. (Sierra Lake Reserve v. City of Rocklin (9th Cir.1991) 938 F.2d 951, 958, vacated in part (1993) 987 F.2d 662; see also Guaranty Nat. Ins. Co. v. Gates (9th Cir.1990) 916 F.2d 508, 515.) For example, if a landlord retrofits an older building in order to comply with new building code requirements, the capital improvements may be the larger part of the building's value. In that case, if fair return did not take those capital improvements into consideration, it would be an empty promise. As the high court noted in Duquesne Light Co. v. Barasch (1989) 488 U.S. 299, 310, 109 S.Ct. 609, 617, 102 L.Ed.2d 646 (Duquesne), "fair rate of return" depends on "the amount of capital upon which the investors are entitled to earn that return." (See also Hope Gas, supra, 320 U.S. at p. 603, 64 S.Ct. at p. 288 ["return ... should be sufficient ... to attract capital"].) Thus, a rent control law that merely allows a landlord to recoup the bare cost of a necessary capital improvement runs the risk of ***680** being confiscatory and thereby violating the landlord's right to due process of law.

Taking of Property Without Just Compensation

[13] The state and federal Constitutions prohibit government from taking private property for public use without just compensation. (Cal. Const., art. I, § 19; U.S. Const., 5th Amend.; Chicago,

Burlington & Q.R. Co. v. Chicago (1897) 166 U.S. 226, 239, 17 S.Ct. 581, 585-586, 41 L.Ed. 979 [applying the federal takings clause to the states].) In Pa. Coal Co. v. Mahon (1922) 260 U.S. 393, 415, 43 S.Ct. 158, 160, 67 L.Ed. 322 (Pa. Coal), the United States Supreme Court recognized that a regulation of property that "goes too far" may effect a taking of that property, though its title remains in private hands. In such a case, the property owner may bring an inverse condemnation action, and if it prevails, the regulatory agency must either withdraw the regulation or pay just compensation. (First Lutheran Church v. Los Angeles County (1987) 482 U.S. 304, 317, 321, 107 S.Ct. 2378, 2387, 2389, 96 L.Ed.2d 250.) Even if the agency withdraws the regulation, the property owner may have a right to just compensation for the temporary taking while the regulation was in effect. (Id. at p. 321, 107 S.Ct. at p. 2389 [finding this right "where the government's activities have ... worked a taking of all use of property"].)

The United States Supreme Court has struggled to articulate a standard for when a regulation "goes too far" and effects a taking. The court has stated broadly that the takings clause is "designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." (Armstrong v. United States (1960) 364 U.S. 40, 49, 80 S.Ct. 1563, 1569, 4 L.Ed.2d 1554.) Nevertheless, the court has concluded that the inquiry in any particular case is "essentially ad hoc" (Penn Central Transp. Co. v. City of New York (1978) 438 U.S. 104, 124, 98 S.Ct. 2646, 2659, 57 L.Ed.2d 631 (Penn Central)) and "a question of degree [that] ... cannot be disposed of by general propositions" (Pa. Coal, supra, 260 U.S. at p. 416, 43 S.Ct. at p. 160). The court has, however, identified "two discrete categories of regulatory action" that constitute a taking. (Lucas v. South Carolina Coastal Council (1992) 505 U.S. 1003, 1015, 112 S. Ct. 2886, 2893, 120 L.Ed.2d 798 (Lucas).) Thus, the court has held that a permanent physical invasion of property, no matter how slight, effects a taking requiring compensation. (Loretto v. Teleprompter Manhattan CATV Corp. (1982) 458 U.S. 419, 421, 102 S.Ct. 3164, 3168, 73 L.Ed.2d 868.) Similarly, the court has held that a regulation that deprives a property owner of "all economically beneficial or productive use of land" effects a taking requiring just compensation. (Lucas, supra, 505 U.S. at p. 1015, 112 S.Ct. at p. 2893; Agins v.

Tiburon (1980) 447 U.S. 255, 260, 100 S.Ct. 2138, 2141, 65 L.Ed.2d 106.)

[14] A regulation, however, may effect a taking though, as is true here, it does not involve a physical invasion and leaves the property owner some economically beneficial use of his property. In Lucas, the high court expressly rejected the "assumption that the landowner whose deprivation is one step short of complete is not entitled to compensation." (Lucas, supra, 505 U.S. at p. 1019, fn. 8, 112 S.Ct. at p. 2895, fn. 8.) "Such an owner" merely lost "the benefit of [the court's] categorical formulation." (Ibid.; see also Nollan v. California Coastal Comm'n (1987) 483 U.S. 825, 831, 107 S.Ct. 3141, 3145-3146, 97 L.Ed.2d 677 (Nollan).) Of course, we held in Agins v. City of Tiburon (1979) 24 Cal.3d 266, 277, 157 Cal.Rptr. 372, 598 P.2d 25, "that a zoning ordinance may be unconstitutional ... only when its effect is to deprive the landowner of substantially all reasonable use of his property." (See also Fisher, supra, 37 Cal.3d at p. 686, 209 Cal.Rptr. 682, 693 P.2d 261 [paraphrasing and citing Agins v. City of Tiburon].) But the regulation at issue in Agins v. City of Tiburon left the plaintiffs a substantial use of their five-acre property, including building as many as five single-family homes on it. In order to uphold the regulation, we did not need to limit the protections of the takings clause to total deprivations of "substantially all reasonable use" of property, because the case before us did not even approach a total deprivation. Thus, our holding was dictum. Moreover, Lucas makes clear we misinterpreted ***681** the federal Constitution, and nothing in our opinion in Agins v. City of Tiburon suggests we were interpreting the state takings clause more narrowly than the federal clause. Finally, even if we did intend to interpret the state right more narrowly than the federal right, the federal Constitution would nevertheless apply here to protect Kavanau.

[15] When a regulation does not result in a physical invasion and does not deprive the property owner of all economic use of the property, a reviewing court must evaluate the regulation in light of the "factors" the high court discussed in Penn Central and subsequent cases. Penn Central emphasized three factors in particular: (1) "[t]he economic impact of the regulation on the claimant"; (2) "the extent to which the regulation has interfered with distinct investment-backed expectations"; and (3) "the character of the governmental action." (Penn Central, supra, 438 U.S. at p. 124, 98 S.Ct. at p. 2659;

MacDonald, Sommer & Frates v. Yolo County (1986) 477 U.S. 340, 349, 106 S.Ct. 2561, 2566, 91 L.Ed.2d 285; Kaiser Aetna v. United States (1979) 444 U.S. 164, 175, 100 S.Ct. 383, 390, 62 L.Ed.2d 332.) Subsequent cases, as well as a close reading of Penn Central, indicate other relevant factors: (1) whether the regulation "interfere[s] with interests that [are] sufficiently bound up with the reasonable expectations of the claimant to constitute 'property' for Fifth Amendment purposes" (Penn Central, supra, 438 U.S. at p. 125, 98 S.Ct. at pp. 2659-2660); (2) whether the regulation affects the existing or traditional use of the property and thus interferes with the property owner's "primary expectation" (id. at pp. 125, 136, 98 S.Ct. at pp. 2659-2660, 2665); (3) "the nature of the State's interest in the regulation" (Keystone Bituminous Coal Assn. v. DeBenedictis (1987) 480 U.S. 470, 488, 107 S.Ct. 1232, 1243, 94 L.Ed.2d 472 (Keystone); see also Mugler v. Kansas (1887) 123 U.S. 623, 668-669, 8 S.Ct. 273, 300-301, 31 L.Ed. 205) and, particularly, whether the regulation is "reasonably necessary to the effectuation of a substantial public purpose" (Penn Central, supra, 438 U.S. at p. 127, 98 S.Ct. at p. 2660); (4) whether the property owner's holding is limited to the specific interest the regulation abrogates or is broader (id. at pp. 127-128, 98 S.Ct. at pp. 2660-2661); (5) whether the government is acquiring "resources to permit or facilitate uniquely public functions" such as government's "entrepreneurial operations" (id. at pp. 128, 135, 98 S.Ct. at pp. 2661, 2664-2665); (6) whether the regulation "permit[s the property owner] ... to profit [and] ... to obtain a 'reasonable return' on ... investment" (id. at p. 136, 98 S.Ct. at p. 2665); (7) whether the regulation provides the property owner benefits or rights that "mitigate whatever financial burdens the law has imposed" (id. at p. 137, 98 S.Ct. at p. 2666; Keystone, supra, 480 U.S. at p. 491, 107 S.Ct. at p. 1245; Agins v. Tiburon, supra, 447 U.S. at p. 262, 100 S.Ct. at p. 2142); (8) whether the regulation "prevent[s] the best use of [the] land" (Ibid.); (9) whether the regulation "extinguish[es] a fundamental attribute of ownership" (ibid.); and (10) whether the government is demanding the property as a condition for the granting of a permit (Dolan v. City of Tigard (1994) 512 U.S. 374, 385, 114 S.Ct. 2309, 2316-2317, 129 L.Ed.2d 304 (Dolan); Nollan, supra, 483 U.S. at pp. 831, 841, 107 S.Ct. at pp. 3145-3146, 3150- 3151).

This list is not a comprehensive enumeration of all the factors that might be relevant to a takings claim, and we do not propose a single analytical method for these claims. Rather, we simply note factors the high court has found relevant in particular cases. Thus, instead of applying these factors mechanically, checking them off as it proceeds, a court should apply them as appropriate to the facts of the case it is considering. Recent Supreme Court decisions suggest a two-part analysis that considers the economic effects of the regulation and the government's purpose. (Yee v. Escondido (1992) 503 U.S. 519, 523, 112 S. Ct. 1522, 1526, 118 L.Ed.2d 153; Keystone, supra, 480 U.S. at pp. 484-485, 107 S.Ct. at pp. 1241-1242.) With respect to the latter consideration, the high court has declared that a regulation of property "effects a taking if [it] does not substantially advance legitimate state interests." (Agins v. Tiburon, supra, 447 U.S. at p. 260, 100 S.Ct. at p. ***682** 2141; see also Dolan, supra, 512 U.S. at p. 385, 114 S. Ct. at pp. 2316-2317; Lucas, supra, 505 U.S. at p. 1016, 112 S.Ct. at pp. 2893-2894; Nollan, supra, 483 U.S. at p. 834, 107 S.Ct. at p. 3147; Keystone, supra, 480 U.S. at p. 485, 107 S.Ct. at pp. 1241- 1242; United States v. Riverside Bayview Homes, Inc. (1985) 474 U.S. 121, 126, 106 S.Ct. 455, 458-459, 88 L. Ed.2d 419.) But, outside the context of permit condition cases such as Nollan and Dolan, the court has not clarified how it would apply this standard, and, in particular, the extent to which it would apply the standard in the same way as the similarly worded due process standard. (Cf. Nollan, supra, 483 U.S. at p. 834, fn. 3, 107 S.Ct. at p. 3147, fn. 3 [stating that the standards are "quite different"]; Dolan, supra, 512 U.S. at p. 391, 114 S.Ct. at pp. 2319-2320 [articulating a " 'rough proportionality' " standard for permit condition cases].)

Penn Central, supra, 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631, of course did not involve a price regulation. In the context of price regulation, the high court has sometimes employed an analysis under the takings clause similar to that which it employs under the due process clause, focusing on the regulation's impact and investors' ability to earn a fair return. In Duquesne, for example, an electric utility argued that electricity rates constituted a taking because the rate-setting agency did not include certain costs in the rate base. (Duquesne, supra, 488 U.S. at p. 305, 109 S.Ct. at p. 614.) Though the court was addressing a takings issue, it did not cite Penn Central.

Instead, it cited due process cases, including Permian Basin, supra, 390 U.S. 747, 88 S.Ct. 1344, 20 L.Ed.2d 312, Hope Gas, supra, 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333, and Pipeline Co., supra, 315 U.S. 575, 62 S.Ct. 736, 86 L.Ed. 1037, and applied a "fair return" analysis similar to the analysis it had traditionally applied in due process cases. (Duquesne, supra, 488 U.S. at pp. 307-310, 109 S.Ct. at pp. 615-617; see also FCC v. Florida Power Corp. (1987) 480 U.S. 245, 250-254, 107 S.Ct. 1107, 1111-1113, 94 L.Ed.2d 282 (Florida Power) [also applying what appears to be a due process analysis when reviewing a price regulation under the takings clause]; 20th Century, supra, 8 Cal.4th at pp. 292-296, 32 Cal.Rptr.2d 807, 878 P.2d 566 [same]; Cotati, supra, 148 Cal.App.3d at p. 293, 195 Cal.Rptr. 825 [a breach of the due process clause in the context of rent control "might well violate" the takings clause]; 2 Rotunda & Nowak, Treatise on Constitutional Law (2d ed.1992) § 15.12, p. 505, fn. 59 ["Early Supreme Court opinions concerning utility rate regulation were written in terms of 'due process of law', but those opinions are now understood as establishing principles identical to those inherent in the takings clause...."]; Brauneis, "The Foundation of Our 'Regulatory Takings' Jurisprudence": The Myth and Meaning of Justice Holmes's Opinion in Pennsylvania Coal Co. v. Mahon (1996) 106 Yale L.J. 613, 672, fn. 270 ["More recently, the Court has once again seemed to graft what was originally a due process test of governmental authority onto the Takings Clause ...."]; but see Yee v. Escondido, supra, 503 U.S. at p. 529, 112 S.Ct. at p. 1529 [suggesting that traditional takings clause jurisprudence applies to rent regulations]; Pennell v. San Jose (1988) 485 U.S. 1, 8-14, 108 S.Ct. 849, 855-859, 99 L. Ed.2d 1 [treating the takings clause and the due process clause separately when deciding a constitutional challenge to a rent control law].)

Court of Appeal Decision in Kavanau I

In Kavanau I, the Court of Appeal determined that the Rent Board's application of its 12 percent limit to Kavanau's petition for rent increases was unconstitutional. Though the court did not state whether it found a violation of Kavanau's due process rights or a taking without just compensation, the court applied a due process analysis and relied on our decisions in Calfarm, supra, 48 Cal.3d 805, 258 Cal.Rptr. 161, 771 P.2d 1247, Fisher, supra, 37 Cal.3d 644, 209 Cal.Rptr. 682, 693 P.2d 261, and Birkenfeld, supra, 17 Cal.3d

129, 130 Cal.Rptr. 465, 550 P.2d 1001, which were all due process cases. (Kavanau I, supra, 19 Cal. App.4th at pp. 734- 735, 23 Cal. Rptr.2d 724.) Thus, we conclude the court did not find a taking.

We question some of the Court of Appeal's reasoning in Kavanau I. For example, that court implied that the state and federal Constitutions require application of the "fair return ***683** on investment" formula for setting rent ceilings. (Kavanau I, supra, 19 Cal.App.4th at pp. 733, 735, 23 Cal.Rptr.2d 724; for a discussion of the fair return on investment formula, see Guidelines, supra, 35 Rutgers L.Rev. at pp. 790- 796.) Though we have used the phrase "just and reasonable return" (Birkenfeld, supra, 17 Cal.3d at p. 165, 130 Cal.Rptr. 465, 550 P.2d 1001), we have never held that either the state or federal Constitution requires application of the fair return on investment formula or any other specific formula. (Fisher, supra, 37 Cal.3d at p. 681, 209 Cal. Rptr. 682, 693 P.2d 261 [rejecting argument that Constitution requires application of the circular "fair return on market value" formula]; Carson, supra, 35 Cal.3d at p. 191, 197 Cal. Rptr. 284, 672 P.2d 1297.)

In addition, rather than amortizing the costs of Kavanau's capital improvements over their useful life, the Court of Appeal apparently treated those costs in the same way as ongoing operating or maintenance costs. (Kavanau I, supra, 19 Cal.App.4th at p. 736, fn. 7, 23 Cal.Rptr.2d 724.) The court also apparently included as capital improvement costs certain expenditures the Rent Board had found unnecessary. (Ibid.) As a result, the court determined that Kavanau incurred a large deficit.

[16][17] Moreover, the Court of Appeal assumed the City's maintenance of net operating income formula without the 12 percent limit established the minimum "fair return" under the state and federal Constitutions. (Kavanau I, supra, 19 Cal. App. 4th at p. 733, 23 Cal.Rptr.2d 724.) Based on this assumption, the Court of Appeal concluded the 12 percent limit put Kavanau's return below the constitutional minimum. But the court did not explain why the 12 percent limit could not be one aspect of a comprehensive scheme that as a whole provided landlords a fair return. (Cf. Pennell v. San Jose, supra, 485 U.S. at pp. 13-14, 108 S.Ct. at pp. 858-859.) "The economic judgments required in rate proceedings are often hopelessly complex.... The Constitution is not designed to arbitrate these

economic niceties." (Duquesne, supra, 488 U.S. at p. 314, 109 S.Ct. at p. 619.) Thus, courts do not "examine[ ] piecemeal" the "subsidiary aspects of [a state agency's] ratemaking methodology" (id. at p. 313, 109 S.Ct. at pp. 618-619), and flexibility in one part of a regulatory scheme may offset restrictiveness in another (id. at p. 314, 109 S.Ct. at p. 619). We see no reason why a reasonable annual limit on rent increases cannot be consistent with a fair return.

Furthermore, the City could have prohibited certain capital improvements altogether, perhaps as a way of keeping a stock of housing available for low income residents. Thus, the City could at its option permit those capital improvements, but encourage landlords to limit their magnitude by prohibiting rent increases in excess of 12 percent per year regardless of the improvements' cost. (Cf. Nollan, supra, 483 U.S. at pp. 836-837, 107 S.Ct. at pp. 3148-3149.)

[18] Finally, the essential inquiry in due process cases involving price controls is whether the regulatory scheme's result is just and reasonable. (Hope Gas, supra, 320 U.S. at p.602, 64 S.Ct. at pp. 287-288.) The Court of Appeal did not expressly find that the 12 percent limit prevented Kavanau from " 'operating successfully.' " (20th Century, supra, 8 Cal.4th at p. 295, 32 Cal.Rptr.2d 807, 878 P.2d 566.) Rather, the 12 percent limit merely delayed Kavanau's rent increase. Regulated prices must fall within a "broad zone of reasonableness" to be constitutional (Permian Basin, supra, 390 U.S. at p. 770, 88 S.Ct. at pp. 1361-1362; see also Pipeline Co., supra, 315 U.S. at p. 585, 62 S.Ct. at pp. 742-43), and due process requires fundamentally a balancing of interests (Hope Gas, supra, 320 U.S. at p. 603, 64 S.Ct. at p. 288). The 12 percent limit achieved this balance. It balanced landlords' interests in recouping their increased costs against tenants' interests in avoiding sudden, large rent increases. Of course, in certain circumstances-- such as during times of very high inflation--a 12 percent limit on rent increases might be confiscatory, but the Court of Appeal did not adequately explain why application of the 12 percent limit to Kavanau's petition for rent increases violated his constitutional rights.

[19] Thus we have serious doubts about the Court of Appeal's reasoning in Kavanau ***684** I. Nevertheless, the Court of Appeal's judgment in that case is final and precludes relitigation of certain issues in this proceeding. (See, e.g., Perez v. City of San Bruno

(1980) 27 Cal. 3d 875, 883, 168 Cal.Rptr. 114, 616 P.2d 1287.) For example, we must accept as true for purposes of this proceeding that application of the Rent Board's 12 percent limit on rent increases violated Kavanau's right to due process of law. Of course, Kavanau obtained a remedy in the form of a writ of mandate, but he also seeks damages.

Kavanau's Present Claim for Damages

In Hensler v. City of Glendale (1994) 8 Cal.4th 1, 14, 32 Cal. Rptr.2d 244, 876 P.2d 1043, we held that, if a property owner brings a timely action to set aside or void a regulation, he may but need not join a claim for damages. Instead, he may bring a damages claim separately after successfully challenging the regulation. (Id. at pp. 7, 26, 32 Cal.Rptr.2d 244, 876 P.2d 1043.) Thus, in Hensler we identified an exception to the general rule against splitting claims. (See also Healing v. California Coastal Com. (1994) 22 Cal. App.4th 1158, 1170, 27 Cal. Rptr.2d 758; Mata v. City of Los Angeles (1993) 20 Cal. App.4th 141, 149, 24 Cal. Rptr.2d 314; Patrick Media Group, Inc. v. California Coastal Com. (1992) 9 Cal.App.4th 592, 607, 11 Cal.Rptr.2d 824; Gallagher v. Frye (9th Cir.1980) 631 F.2d 127, 130.) In accordance with Hensler, Kavanau brought his present claim for damages, alleging two causes of action.

In his second cause of action, Kavanau sought damages based on the violation of his right to due process. The state and federal due process clauses, unlike the takings clauses, make no express reference to damages, but Kavanau alleged a "deprivation of ... rights, privileges, or immunities secured by the Constitution," entitling him to damages under section 1983. We need not determine whether section 1983 would allow Kavanau to recoup damages under the facts of this case, because he abandoned his section 1983 cause of action, choosing instead "[t]o focus attention on what [he] believes to be the important constitutional questions involved ... [in] his first cause of action for inverse condemnation...." The Court of Appeal expressly noted that Kavanau had abandoned the section 1983 cause of action, and he did not petition for rehearing. Accordingly, the only cause of action before us is Kavanau's first cause of action alleging a taking and seeking just compensation. (See Cal. Rules of Court, rule 29(b).)

[20][21] Kavanau's allegations, if true, are not sufficient to establish a taking, and therefore the trial court was correct to sustain

the Rent Board's demurrer. This case does not fall within either of the "two discrete categories of regulatory action" that constitute a taking. (Lucas, supra, 505 U.S. at p. 1015, 112 S.Ct. at p. 2893; Agins v. Tiburon, supra, 447 U.S. at p. 260, 100 S.Ct. at p. 2141.) Rent control does not generally constitute a physical invasion of property (Yee v. Escondido, supra, 503 U.S. 519, 112 S.Ct. 1522, 118 L.Ed.2d 153), and we agree with the Court of Appeal that Kavanau has not lost "all economically beneficial or productive use of" his property (Lucas, supra, 505 U.S. at p. 1015, 112 S.Ct. at p. 2893).

[22] Nor do the factors the high court articulated in Penn Central and subsequent cases indicate a taking in this case. The "economic impact" (Penn Central, supra, 438 U.S. at p. 124, 98 S.Ct. at p. 2659) on Kavanau of the 12 percent limit, which in effect merely delayed his rent increase, was not significant when compared to the benefits he continued to receive from his property, including significant rental income (id. at p. 130, 98 S.Ct. at p. 2662 [rejecting assertion that a reviewing court should consider the property interest that a regulation affects in isolation from unaffected property interests]). Similarly, the "interfere[nce] with [Kavanau's] distinct investment-backed expectations" (id. at p. 124, 98 S. Ct. at p. 2659) was minor, considering he had constructive knowledge of the 12 percent limit when he chose to improve his property. Finally, the "character of the governmental action" (ibid.) does not compel us to find a taking.

This case does not involve a regulation that "prohibited a beneficial use to which [Kavanau's building] had previously been devoted" (Penn Central, supra, 438 U.S. at p. 125, 98 S.Ct. at pp. 2659-2660), thus interfering with ***685** Kavanau's "primary expectation" (id. at p. 136, 98 S.Ct. at p. 2665). Rather, the 12 percent limit affected Kavanau largely because he changed the use of his building by making costly capital improvements. Nor did the 12 percent limit abrogate Kavanau's entire property holding, as might occur when someone owns only mineral rights and a land-use regulation prohibits mining those minerals. (Pa. Coal, supra, 260 U.S. at pp. 412-416, 43 S.Ct. at pp. 159-160; Penn Central, supra, 438 U.S. at pp. 127-128, 98 S. Ct. at pp. 2660-2661.) Furthermore, by imposing the 12 percent limit, the Rent Board was not acquiring "resources to permit or facilitate uniquely public functions" such as government's "entrepreneurial operations." (Penn Central,

supra, 438 U.S. at pp. 128, 135, 98 S.Ct. at pp. 2661, 2664-2665.) Nor did the 12 percent limit "prevent the best use" of Kavanau's building or "extinguish a fundamental attribute of ownership." (Agins v. Tiburon, supra, 447 U.S. at p. 262, 100 S.Ct. at p. 2142.) In addition, the Rent Board did not impose the 12 percent limit as a condition for granting a permit. (Dolan, supra, 512 U.S. at p. 385, 114 S.Ct. at pp. 2316- 2317; Nollan, supra, 483 U.S. at pp. 831, 841, 107 S.Ct. at pp. 3145-3146, 3150-3151.) Finally, the Rent Board has a "legitimate ... interest[ ]" in easing the burden on tenants of sudden, large rent increases, and the 12 percent limit "substantially advance[d]" that interest. (Agins v. Tiburon, supra, 447 U.S. at p. 260, 100 S.Ct. at p. 2141; see also Penn Central, supra, 438 U.S. at p. 127, 98 S.Ct. at pp. 2660- 2661; Keystone, supra, 480 U.S. at p. 488, 107 S.Ct. at pp. 1243- 1244.) Thus, the factors that have proved relevant in other takings cases do not indicate a taking in this case.

[23] But Kavanau emphasizes the Court of Appeal's finding in Kavanau I that application of the 12 percent limit deprived him of a fair return and thus violated his right to due process. We must, of course, accept that finding as true for purposes of this proceeding. Put simply, Kavanau argues that, because he lost rental income as a direct result of the Rent Board's unconstitutional application of its 12 percent limit, he has suffered a taking requiring just compensation. Thus, Kavanau asks us to consider whether a rent regulation that violates a particular property owner's right to due process by depriving him of a fair return also necessarily constitutes a taking.

As noted, the United States Supreme Court has declared that a regulation of property "effects a taking if [it] does not substantially advance legitimate state interests." (Agins v. Tiburon, supra, 447 U.S. at p. 260, 100 S.Ct. at p. 2141.) The similarity of this takings standard to the due process requirement that a regulation "have a reasonable relation to a proper legislative purpose" (Nebbia, supra, 291 U.S. at p. 537, 54 S.Ct. at p. 516) supports Kavanau's argument that a due process violation in this context constitutes a taking. In fact, when the high court first articulated this takings standard, it cited Nectow v. Cambridge (1928) 277 U.S. 183, 188, 48 S.Ct. 447, 448, 72 L.Ed. 842, a due process case. (Agins v. Tiburon, supra, 447 U.S. at p. 260, 100 S.Ct. at p. 2141.) Kavanau's argument might also find some support in cases such as Duquesne,

supra, 488 U.S. 299, 109 S.Ct. 609, 102 L.Ed.2d 646, Florida Power, supra, 480 U.S. 245, 107 S.Ct. 1107, 94 L.Ed.2d 282 (1987), and 20th Century, supra, 8 Cal.4th 216, 32 Cal.Rptr.2d 807, 878 P.2d 566, which apply standards under the takings clause similar to those that apply under the due process clause.

On the other hand, the Rent Board stresses the distinct functions of the due process clause and the takings clause. The Rent Board argues that the due process protection focuses on method. It requires that a regulation not be arbitrary or capricious and that the regulatory agency give due consideration to conflicting interests. The takings protection focuses on result. According to the Rent Board, a taking occurs only in cases of " 'deep financial hardship' " (20th Century, supra, 8 Cal.4th at p. 258, 32 Cal.Rptr.2d 807, 878 P.2d 566) or when a regulation deprives a property owner of nearly all use of the property (Lucas, supra, 505 U.S. at p. 1015, 112 S.Ct. at p. 2893). The Rent Board asserts we should no more treat a due process violation affecting property as a taking than we would treat an equal protection or free speech violation affecting property as a taking.

***686** [24][25] In this case, we need not decide whether a rent regulation that violates a particular property owner's right to due process also constitutes a taking, because, assuming it otherwise might, we hold that a remedy for the due process violation, if available and adequate, obviates a finding of a taking. In a variety of contexts, the Supreme Court has recognized that the benefits a property owner receives in conjunction with a regulation may offset the burdens and thus satisfy the takings clause. (Penn Central, supra, 438 U.S. at p. 137, 98 S.Ct. at pp. 2665- 2666; see generally Kendall & Ryan, "Paying" for the Change: Using Eminent Domain to Secure Exactions and Sidestep Nollan and Dolan (1995) 81 Va. L.Rev. 1801, 1837-1842; Costonis, "Fair" Compensation and the Accommodation Power: Antidotes for the Taking Impasse in Land Use Controversies (1975) 75 Colum. L.Rev. 1021, 1039-1042.) Thus, in Pa. Coal, Justice Holmes noted the "average reciprocity of advantage" that often characterizes regulations and justifies them for purposes of the takings clause. (Pa. Coal, supra, 260 U.S. at p. 415, 43 S. Ct. at p. 160.) More explicitly, the court has long held that the special benefits conferred on a property owner's remaining property as a direct result of a taking may constitute just compensation. (Bauman v. Ross (1897) 167 U.S. 548, 17 S.Ct. 966, 42 L.Ed. 270.)

Bauman involved the taking of private property to build a highway in the District of Columbia. The court stated: "The Constitution of the United States contains no express prohibition against considering benefits in estimating the just compensation to be paid for private property taken for the public use; and ... no such prohibition can be implied...." (Id. at p. 584, 17 S. Ct. at p. 980.) Similarly, a government agency may "mitigate ... [the] financial burdens" of a land-use regulation, and thus avoid a takings clause violation, by transferring development rights to the property owner's other parcels. (Penn Central, supra, 438 U.S. at p. 137, 98 SCt. at pp. 2665-2666; see also MacDonald, Sommer & Frates v. Yolo County, supra, 477 U.S. at p. 350, 106 S.Ct. at pp. 2566- 2567; cf. Suitum v. Tahoe Regional Planning Agency (1997) --- U.S. ----, 117 S.Ct. 1659, 137 L.Ed.2d 980 [not deciding whether the sale value of transferable development rights is relevant to the existence of a taking or only to the adequacy of the compensation].) Consistent with the reasoning of these cases, when a due process violation is the sole basis of an asserted taking, a remedy for the due process violation, if available and adequate, is a valuable benefit that satisfies the takings clause. (Cf. Williamson Planning Comm'n v. Hamilton Bank (1985) 473 U.S. 172, 194-197, 105 S.Ct. 3108, 3120-3122, 87 L.Ed.2d 126 [state law inverse condemnation remedy may be adequate compensation for purposes of takings clause]; Ruckelshaus v. Monsanto Co. (1984) 467 U.S. 986, 1019, 104 S.Ct. 2862, 2881, 81 L.Ed.2d 815 [Tucker Act remedy may be adequate compensation for purposes of takings clause]; Regional Rail Reorganization Act Cases (1974) 419 U.S. 102, 136, 150, 155-156, 95 S.Ct. 335, 354-355, 362, 364-365, 42 L. Ed.2d 320 [same].)

Under the due process clause, future rent ceilings must enable Kavanau to earn a fair return that will "maintain financial integrity, attract necessary capital, and fairly compensate [him] for the risks [he has] assumed." (Permian Basin, supra, 390 U.S. at p. 792, 88 S.Ct. at p. 1373.) Among other things, this standard requires the Rent Board to consider, when setting rent ceilings, Kavanau's costs, which include certain costs associated with rent control. (Civ.Code, § 1947.15 [stating circumstances in which rent control agencies must consider the cost to a landlord of professional services associated with rent control].) We think one of the costs associated with rent control that the Rent Board must consider is the cost to Kavanau of

any confiscatory rent ceilings the Rent Board previously imposed on the apartments in question. (Cf. Communications Satellite Corp. v. F.C.C. (D.C.Cir.1977) 611 F.2d 883, 894 & fn. 19 [past deficiency "may not be capitalized into the rate base for future years" unless "rates ... have for some time been under strictures set by an administrative agency" and the deficiency is the result of agency "miscalculation"].) Thus, irrespective of whether section 1983 would have afforded Kavanau a remedy for the due process violation, his continuing right to an adjustment of future rents can provide an adequate remedy.

***687** An adjustment of future rents that takes into consideration past confiscatory rents is the converse of the refund that producers in price- regulated industries may have to pay if, during litigation over price levels, they charge prices that a court later determines to be excessive. (See, e.g., Trans Alaska Pipeline Rate Cases (1978) 436 U.S. 631, 655, 98 S. Ct. 2053, 2066-2067, 56 L. Ed.2d 591.) Moreover, this remedy, as opposed to an award of damages against the Rent Board, places the cost of compensating Kavanau roughly on those tenants who benefited from unconstitutionally low rents. (Cf. State of California v. Levi Strauss & Co. (1986) 41 Cal.3d 460, 472-473, 224 Cal.Rptr. 605, 715 P.2d 564 [antitrust class action applying "fluid recovery" whereby fund roughly benefits those who suffered damages]; Blue Chip Stamps v. Superior Court (1976) 18 Cal.3d 381, 388, fn. 1, 134 Cal.Rptr. 393, 556 P.2d 755 (conc. opn. of Tobriner, J.) [price reduction as remedy for overcharges].) We note in this regard that if any of Kavanau's tenants have vacated an apartment, then state law may have authorized Kavanau to set the rent for his new tenants at a level that enabled him, or will enable him, to recoup past losses. (Civ.Code, §§ 1954.50-1954.53.) In that case, he would not be entitled to an additional rent adjustment. Thus, in practice, future rent adjustments are likely to affect only those tenants who have not moved and who benefited from unconstitutionally low rents.

[26] Finally, the remedy of future rent adjustments avoids putting a reviewing court in the position of declaring the appropriate regulated rent ceiling for a particular apartment in order to measure damages. (Cf. United States v. Western Pac. R. Co. (1956) 352 U.S. 59, 63-64, 77 S.Ct. 161, 164-165, 1 L.Ed.2d 126 [deferring to the "primary jurisdiction" of an administrative agency "whenever

enforcement of the claim requires the resolution of issues which ... have been placed within the special competence of an administrative body"].) Setting rent ceilings is essentially a legislative task, and agencies, not courts, choose which administrative formula to apply. (Fisher, supra, 37 Cal.3d at p. 681, 209 Cal.Rptr. 682, 693 P.2d 261.) The state and federal Constitutions require only a fair process that reasonably takes into consideration the landlord's interests, and a landlord's return need only fall within a "broad zone of reasonableness." (Permian Basin, supra, 390 U.S. at p. 770, 88 S.Ct. at pp. 1361- 1362). Accordingly, courts are in no position to determine the appropriate rent ceiling for an apartment as a means of assessing damages. We strongly resist any rule that would impose on a reviewing court the impossible task of finding somewhere in the penumbra of the Constitution a stipulation that a particular apartment in a particular building should rent for $746 per month rather than $745.

[27] Here, the City's rent control scheme is sufficiently flexible to permit the Rent Board to consider past confiscatory rent ceilings when evaluating a landlord's petition for a rent increase. (Charter, § 1805(e).) Kavanau, of course, is not necessarily entitled to rent increases equal to the exact amount by which his past rents fell below some imagined constitutional minimum. Rather, he is merely entitled to future rent ceilings that will "maintain financial integrity, attract necessary capital, and fairly compensate [him] for the risks [he has] assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable." (Permian Basin, supra, 390 U.S. at p. 792, 88 S.Ct. at p. 1373.) But, in measuring the future rent ceiling for a particular apartment, the Rent Board must take into consideration the effect on Kavanau, if any, of the temporary enforcement of its confiscatory regulation with respect to that apartment. In this regard, we note Kavanau's actual loss in this case may be small or nonexistent. For example, the Rent Board arguably could have satisfied the Kavanau I mandate by waiving the 12 percent limit, but imposing a higher limit, under some other regulatory provision, that adequately accommodated Kavanau's interest in a fair return. If, in response to Kavanau I, the Rent Board allowed Kavanau to increase rent in accordance with its maintenance of net operating income formula, but without any annual limit, it may already have enabled Kavanau to recoup his losses. In addition, the

12 percent limit was not confiscatory to the extent *688 market conditions would have prevented Kavanau from increasing rent more than 12 percent even if the Rent Board had not enforced the limit.

Kavanau asserts he would have to double his rents in order to recoup his losses within a reasonable period of time. He points out that he operates in a competitive environment, and he argues that future rent adjustments are an inadequate remedy because they will price his apartments above market levels and leave him with an empty building. If Kavanau's assertion is true, then those same market forces might well have prevented Kavanau from increasing his rents regardless of the 12 percent limit. The Constitution does not protect investors from the risks inherent in the marketplace. In addition, Kavanau does not persuade us that his losses, if any, are so great as to prevent him from recouping them through future rent adjustments. In fact, Kavanau conceded at oral argument that his rents remained well below free market levels even with the full increase he sought. Moreover, if a landlord acts promptly to challenge a confiscatory regulation, and seeks a stay of that regulation during litigation, his losses, and thus any future rent adjustments, are likely to be relatively small. A landlord who unnecessarily permits large losses to accumulate cannot complain if the market prevents him from recouping those losses. Finally, we do not here decide what alternative remedy might be appropriate if a landlord can establish that the remedy of future rent adjustments is for some reason unavailable. But before Kavanau can allege the unavailability of future rent adjustments, he must petition for those adjustments, the Rent Board must determine, subject to judicial review, their appropriate amount, and he must attempt to impose them.

[28] Just as a reviewing court averages the effects of subsidiary aspects of a price-setting scheme by looking at "net effect" (Duquesne, supra, 488 U.S. at p. 314, 109 S.Ct. at p. 619), a reviewing court can also average the effects of a price-setting scheme over time. Thus, a fair return over the course of several years will offset a confiscatory return during a particular year. Recognizing that Kavanau has a continuing right under the due process clause to future rent adjustments that will enable him to earn a fair return, we believe he has not suffered a taking. Put another way, the ongoing process of setting rent ceilings dispels the due process violation, which in this

case is the sole basis for a potential takings clause violation. (Cf. Mountain Water v. Mont. Dept. of Public Serv. Reg. (9th Cir.1990) 919 F.2d 593, 601 [no violation of Constitution because water utility "may seek just compensation for its property taken through [future] rate setting"].) Accordingly, we agree with the trial court and the Court of Appeal that Kavanau has not stated a viable inverse condemnation claim.

CONCLUSION

Kavanau I determined that application of the Rent Board's 12 percent limit on rent increases violated Kavanau's right to due process. The remedy of future rent adjustments available to Kavanau under the due process clause precludes a finding of a taking in this case. Accordingly, we affirm the judgment of the Court of Appeal.

GEORGE, C.J., and MOSK, KENNARD and WERDEGAR, JJ., concur.

MOSK, Justice, concurring.

I concur in the majority opinion. I write separately to attempt further clarification of the relationship between due process and takings jurisprudence in the context of rent control and rate regulation generally.

The term "due process" has at least two distinct meanings or applications in the field of rate regulation: (1) substantive due process, i.e., whether the scheme of regulation in question is " ' "arbitrary, discriminatory, or demonstrably irrelevant to the policy the Legislature is free to adopt...." ' " (Pennell v. San Jose (1988) 485 U.S. 1, 11, 108 S.Ct. 849, 857, 99 L.Ed.2d 1 (Pennell)); (2) what can be termed "confiscatory" due process, i.e. whether a given scheme of rate regulation, although not per se or facially invalid, is confiscatory in its result and has prevented an opportunity to obtain a just and reasonable rate of return on investment. ***689** (See Duquesne Light Co. v. Barasch (1989) 488 U.S. 299, 307-308, 109 S.Ct. 609, 615-616, 102 L.Ed.2d 646 (Duquesne Light Co.)). As explained below, it is this latter confiscatory due process analysis that significantly overlaps the takings clause.

Substantive due process analysis of price and rate regulation is fairly straightforward. Price regulation is presumed to be

constitutional, and " 'The burden of proving' otherwise 'rests on the party asserting the violation....' [Citation.] It 'is not easily met. For the last half-century, courts have upheld challenged governmental acts unless no reasonably conceivable set of facts could establish a rational relationship between the regulation and the government's legitimate ends.' [Citation.] 'It is enough that there is an evil at hand for correction, and that it might be thought that the particular ... measure was a rational way to correct it.' " (20th Century Ins. Co. v. Garamendi (1994) 8 Cal. 4th 216, 292, 32 Cal.Rptr.2d 807, 878 P.2d 566, italics added (20th Century Ins. Co.).)

Rent control is simply a form of price control. "For constitutional purposes rent control is indistinguishable from other types of governmental price regulation. Despite the permanence and concreteness of real property, and the special place accorded it by the common law and expounded by the early commentators, its commercial use is no less subject to regulation under the police power than other, more ephemeral, goods and services.... To ascertain the limitations imposed by the ... federal constitution[ ] upon municipal efforts to regulate rents, it is therefore appropriate to consider the constitutional limits on governmental regulation of prices generally." (Hutton Park Gardens v. Town Council of West Orange (1975) 68 N.J. 543, 350 A.2d 1, 7-8, fn. omitted.)

As the United States Supreme Court affirmed in Pennell, a rent control case: "[W]e have long recognized that a legitimate and rational goal of price or rate regulation is the protection of consumer welfare." (Pennell, supra, 485 U.S. at p. 13, 108 S. Ct. at p. 858.) Thus, that court upheld a facial challenge to a rent control ordinance that "represents a rational attempt to accommodate the conflicting interests of protecting tenants from burdensome rent increases while at the same time ensuring that landlords are guaranteed a fair return on their investment." (Ibid.) Accordingly, the notion advanced by some commentators (see Radford, Regulatory Takings Law in the 1990s: The Death of Rent Control? (1992) 21 Sw. U. L. Rev. 1019) that rent control laws are subject to a heightened constitutional scrutiny that goes beyond the substantive due process "rational relationship" analysis to which other economic regulation is subject, is without constitutional basis. Nor is it constitutionally sound to assert that a trial court, sitting as trier of fact, may act as a kind of "Super City Council" that can evaluate whether a rent control law has

been successful in achieving its stated purposes. (See ibid.) A trial court may not arrogate to itself such a role. Neither may an appellate court. "In a substantive due process challenge, we do not require that the City's legislative acts actually advance its stated purpose, but instead look to whether ' "the governmental body could have had no legitimate reason for its decision." ' " (Kawaoka v. City of Arroyo Grande (9th Cir.1994) 17 F.3d 1227, 1234, italics in original.) Whether rent control is the best way to remedy the problem of excessive rents in a given locale, and whether the benefits it brings in terms of lower-than-market rents for some tenants outweighs its costs, is a matter to be addressed to legislative bodies. [FN1]

FN1. The notion that rent control laws may now be subject to a more exacting form of constitutional scrutiny is predicated on a reading of Nollan v. California Coastal Commission (1987) 483 U.S. 825, 107 S.Ct. 3141, 97 L. Ed.2d 677. (See Radford, supra, 21 Sw. U. L.Rev. at p. 1030.) We have rejected elsewhere the contention that Nollan and the related case of Dolan v. City of Tigard (1994) 512 U.S. 374, 114 S. Ct. 2309, 129 L.Ed.2d 304 represent a new standard of scrutiny of government regulation other than those regulations that require either a physical dedication of property, or a development fee levied on an "individual and discretionary basis." (Ehrlich v. City of Culver City (1996) 12 Cal.4th 854, 876, 50 Cal.Rptr.2d 242, 911 P.2d 429.) In the present case, rent control neither requires a physical dedication nor amounts to an individual and discretionary development fee. Indeed, as explained above, it is not a land use regulation at all but a form of price control.

Moreover, the fact that the Pennell decision, which postdates Nollan, relies on traditional substantive due process analysis in determining whether a rent control law is within a city's police power (Pennell, supra, 485 U.S. at pp. 11-12, 108 S. Ct. at pp. 857-858), indicates that Nollan does nothing to undermine the fundamental constitutional validity of rent control laws. "[W]e have 'consistently affirmed that States have broad power to regulate housing conditions in general and the landlord-tenant relationship in particular without paying compensation for all economic injuries that such regulation entails.' " (Pennell, supra, 485 U.S. at p. 12, fn. 6, 108 S.Ct. at p. 856, fn. 6.) In short, nothing in recent Supreme Court case law indicates an intent to

> replace the traditionally deferential substantive due process standard with some heightened takings standard when reviewing the basic validity of a rent control law or other form of price regulation. And the mere fact that a plaintiff chooses to label his or her action as a suit for just compensation after a "taking," when it is in essence a substantive due process challenge to an economic regulation, is without constitutional significance.

***690** Although a government agency's capacity under the police power to regulate rents in some manner is seldom in doubt, the particular form the regulation takes will not pass constitutional scrutiny if it is confiscatory. This confiscatory analysis, although it also goes under the rubric of "due process," is substantially different than the substantive due process analysis discussed immediately above. The fixing of a " 'just and reasonable' rate [ ] involves a balancing of the investor and the consumer interests.... [T]he investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated." (Federal Power Commission v. Hope Natural Gas Company (1944) 320 U.S. 591, 603, 64 S.Ct. 281, 288, 88 L.Ed. 333 (Hope).) In determining a just and reasonable rate, "it is the result reached not the method employed which is controlling. [Citations.] It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important." (Id. at p. 602, 64 S.Ct. at pp. 287-288.) Thus in Hope, for example, Justice Douglas discussed the utility's historical earnings and financial status in considerable detail and concluded that it was able to maintain its "financial integrity." (Hope, supra, 320 U.S. at pp. 604-605, 64 S.Ct. at pp. 288-289.) The court more recently did the same in Duquesne Light Co., supra, 488 U.S. at page 312, 109 S.Ct. at page 618.

Some rent control cases speak of confiscatory regulations without engaging in "end result" analysis. (See Birkenfeld v. City of Berkeley (1976) 17 Cal.3d 129, 165, 130 Cal.Rptr. 465, 550 P.2d 1001.) In Birkenfeld, we found that Berkeley's rent control law, as then drafted, was partly unconstitutional because it failed to make adequate provision for adjusting base rents. (Id. at p. 169, 130 Cal. Rptr. 465, 550 P.2d 1001.) Although Birkenfeld used the language

of confiscation, it is in fact closer to substantive due process analysis. As we stated: "The provisions [of a rent control law] are within the police power if they are reasonably calculated to eliminate excessive rents and at the same time provide landlords with a just and reasonable return on their property. However, if it is apparent from the face of the provisions that their effect will necessarily be to lower rents more than could reasonably be considered to be required for the measure's stated purpose, they are unconstitutionally confiscatory." (Id. at p. 165, 130 Cal.Rptr. 465, 550 P.2d 1001.) Turning to Berkeley's rent control scheme, we concluded that "Here the [law] drastically and unnecessarily restricts the rent control board's power to adjust rents, thereby making inevitable the arbitrary imposition of unreasonably low rent ceilings." (Id. at p. 169, 130 Cal.Rptr. 465, 550 P.2d 1001.) Thus, this particular feature of Berkeley's scheme was deemed to be constitutionally invalid not because its end result was actually "confiscatory," in the sense in which Hope and its progeny employ that term, but because it was arbitrary and could not be rationally related to the legitimate state purpose of "eliminat[ing] excessive rents and at the same time provid[ing] landlords with a just and reasonable return on their property." (Birkenfeld, supra, 17 Cal.3d at p. 165, 130 Cal. Rptr. 465, 550 P.2d 1001.)

Similarly, regulation that set rates for insurers at less than a fair rate of return in order to compensate for supposedly excess profits was determined to be a violation of *691 due process in Calfarm Ins. Co. v. Deukmejian (1989) 48 Cal.3d 805, 819, 258 Cal.Rptr. 161, 771 P.2d 1247. "[T]he concept that rates may be set at less than a fair rate of return in order to compel the return of past surpluses is not one supported by precedent." (Ibid.) Again, this aspect of the law was declared unconstitutional because it failed to pursue a legitimate state purpose--an essentially substantive due process violation--not because it resulted in fact in the undermining of the financial integrity of the various insurance companies.

In Duquesne Light Co., supra, 488 U.S. 299, 109 S.Ct. 609, 102 L.Ed.2d 646, the court appeared to use the terms "due process" and "taking" interchangeably in referring to utility rate regulation that is confiscatory and therefore constitutionally defective. As the court stated, "[t]he guiding principle has been that the Constitution protects utilities from being limited to a charge for their property serving the public which is so 'unjust' as to be confiscatory. Covington and

Lexington Turnpike Road Co. v. Sandford, 164 U.S. 578, 597, 17 S.Ct. 198, 205, 41 L.Ed. 560 (1896) (A rate is too low if it is 'so unjust as to destroy the value of [the] property for all the purposes for which it was acquired,' and in so doing 'practically deprive[s] the owner of property without due process of law'); [citations]. If the rate does not afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments." (Duquesne Light Co., supra, 488 U.S. at pp. 307-308, 109 S.Ct. at pp. 615-616, italics added.) However, it is clear that the Duquesne Light Co.'s equation of the two constitutional provisions was made only in reference to rate regulations that are confiscatory in their end result. (Duquesne Light Co., supra, 488 U.S. at p. 310, 109 S. Ct. at p. 610.) In other words, a rate regulation is judged to be a taking when its effect has been actually confiscatory, not when it violates substantive due process. As has been stated, "[A]bsent ... deep financial hardship [of a regulated public utility], there is no taking, and ... no obligation to compensate...." (Jersey Central Power and Light Co. v. FERC (1987) 810 F.2d 1168, 1181, fn. 3; accord, 20th Century Ins. Co., supra, 8 Cal.4th at p. 297, 32 Cal.Rptr.2d 807, 878 P.2d 566.)

The notion that a price regulation that leads to the actual confiscation of property is a "taking" of that property is congruent with the Supreme Court's evolving takings jurisprudence in the field of land use law, wherein the impact of land use regulation, either in economic terms or in terms of physical intrusion on real property, is paramount in any takings analysis. (See Lucas v. South Carolina Coastal Council (1992) 505 U.S. 1003, 1015-1016, 112 S.Ct. 2886, 2893-2894, 120 L.Ed.2d 798.) But nothing in the land use cases, or in Duquesne Light Co., suggests that any regulation that violates substantive due process is a taking for which just compensation must be paid. [FN2]

FN2. It is admittedly true that Supreme Court precedent is not entirely clear on where substantive due process ends and takings law begins. In the area of land use regulation, the court has held that a general zoning law is a taking of property if it "does not substantially advance legitimate state interests." (Agins v. City of Tiburon (1980) 447 U.S. 255, 260, 100 S.Ct. 2138, 2141, 65 L. Ed.2d 106.) Whether and to what extent this standard differs from the ordinary substantive due process "rationally related" standard

is a question beyond the scope of this opinion. The "substantially advance" standard has not been applied by the Supreme Court outside the special area of forced dedications of property in exchange for development permits. (See Nollan v. California Coastal Commission, supra, 483 U.S. 825, 107 S.Ct. 3141, 97 L. Ed.2d 677; Dolan v. City of Tigard, supra, 512 U.S. 374, 114 S. Ct. 2309, 129 L.Ed.2d 304.) In any case, the Supreme Court has not indicated any intent to extend the "substantially advance" test beyond the realm of zoning and similar laws which restrict the use of land, and has not applied such a test to price regulations. (See fn. 1, ante).

In the present case, the basis of the Court of Appeal's holding in the original Kavanau decision (see Kavanau v. Santa Monica Rent Control Bd. (1993) 19 Cal. App.4th 730, 23 Cal.Rptr.2d 724 (Kavanau I)) is unclear. The opinion can be read as a substantive due process case, concluding that the 12 percent cap found in the Santa Monica ordinance is arbitrary. As the majority herein explain, however, there is no reason why a 12 percent cap cannot "be one aspect of a comprehensive scheme that as a whole provide[s] landlords *692 a fair return." (Maj. opn., ante, at page 683 of 66 Cal. Rptr.2d, at page ---- of --- P.2d.) It appears from the dollar figures alleged in Earl W. Kavanau's complaint and stated in the majority opinion (maj. opn., ante, at page 676 of 66 Cal.Rptr.2d, at page 855 of 941 P.2d), that Kavanau may have made a bad business decision purchasing the rental property in question, since the amount of debt service and operating expenses exceed rental income. These facts on their face do not indicate a constitutional violation. " 'A regulated firm has no constitutional right to a profit.' " (20th Century Ins. Co., supra, 8 Cal.4th at p. 294, 32 Cal. Rptr.2d 807, 878 P.2d 566, brackets omitted.) Although, as the majority point out, we are bound by the law of the case to the Court of Appeal's conclusion that a 12 percent cap was arbitrary, this conclusion does not signify that Kavanau was in fact subject to "deep financial hardship" as the result of the rent regulation. The judgment of the Kavanau I court does not translate into the claim that Kavanau deserves just compensation under the Fifth Amendment to the United States Constitution.

As the majority properly conclude, the cost of past confiscatory rent regulation is "one of the costs associated with rent control that the Rent Board must consider" in setting a present just and reasonable

rent. (Maj. opn., ante, at page 686 of 66 Cal.Rptr.2d, at page 865 of 941 P.2d.) If Kavanau can establish not only that the 12 percent cap was arbitrary, but that as the result of its imposition, he in fact suffered a sustained period of financial hardship that defeated any reasonable investment-backed expectation for the market in which he operated, then he may be entitled to a rate increase that compensates for such a confiscatory rate. But since, even if Kavanau I is taken at face value, it is far from clear that the result of the Santa Monica Rent Control Board's rate order was the actual imposition of an unfairly low rate of return, and since the post-Kavanau I remedy may have adequately compensated Kavanau for whatever supposed losses he suffered at the hands of the rent board, the majority is correct to conclude that Kavanau may not be entitled to any further rent readjustment. (See maj. opn., ante, at page 687 of 66 Cal. Rptr.2d, at page 866 of 941 P.2d.)

There is yet another reason why a landlord's claim for damages would be, at the very least, vitiated under a scheme of rent regulation. As I stated in my concurring opinion in 20th Century Ins. Co., supra, 8 Cal.4th at page 330, 32 Cal.Rptr.2d 807, 878 P.2d 566, it is evidently the case that " '[a] property owner must be legally compelled to engage in price-regulated activity for regulations to give rise to a taking. [Citations.] For example, public utilities generally are under a state statutory duty to serve the public, and must furnish "service on demand to all applicants" at government-determined rates. [Citations.] Because utilities are compelled to employ their property to provide services to the public, the Fifth Amendment requires regulators to provide utilities with reasonable compensation for their services. [Citations.] [¶] By contrast, where a service provider voluntarily participates in a price-regulated program or activity, there is no legal compulsion to provide service and thus there can be no taking.' " A "voluntary" participation in a price-regulated program is said to occur when an individual or company has the "right to withdraw therefrom." (Id. at p. 331, 32 Cal.Rptr.2d 807, 878 P.2d 566.)

Thus, one who persists in engaging in a regulated activity over an extended period of time, when withdrawal from that activity is an option, cannot lay at the doorstep of government regulation the reason for its economic failure. Government regulation may indeed place some firms in financial jeopardy, but that in itself does not give

rise to a constitutional violation when the government does not block the outflow of assets from these no-longer-profitable enterprises. Some features of the rate regulation may be a violation of substantive due process if they cannot be said to be part of a rational regulatory scheme, and these would therefore be subject to invalidation through injunctive and declaratory relief. But it does not follow that one who has a right to withdraw his capital from the regulated enterprise in question may press a damages claim against the government, either a just compensation claim for a taking or a statutory claim for damages under section 1983 of title 42 of the United States Code. It appears doubtful therefore that a landlord who is subject to lower-than-*693 reasonable rents, and has the option of withdrawing from the rental market, or recouping his previous losses prospectively through a compensatory rent order, can ever press such a claim.

BAXTER, Justice, dissenting.

I respectfully dissent from the majority's holding that a compensable taking cannot occur even though the government, acting through its rent control board, deprives a landlord of the opportunity to earn a fair and reasonable return on the landlord's property through unconstitutional and confiscatory application of its rent control regulations. I share Justice Croskey's view, expressed in his dissent below: "I can perceive of no reason in law or logic why a confiscatory rent control regulation, found to be unconstitutional on due process grounds, would not result in a compensable taking if it were nevertheless enforced and a monetary deprivation resulted. I can imagine no clearer example of a case where compensation should be paid than where the government has illegally taken or diverted to its own social goals the private property of one of its citizens. Indeed, such a common sense result and statement of principle should need no citation of authority."

In a decision now final (Kavanau v. Santa Monica Rent Control Bd. (1993) 19 Cal. App.4th 730, 23 Cal.Rptr.2d 724 (Kavanau I)), the Court of Appeal held that, as a result of the constitutionally impermissible action of defendant Santa Monica Rent Control Board, plaintiff was denied a fair and reasonable return on his rental property. As a result he allegedly suffered damages of $113,095 as of the date of his complaint. He sought to recover that amount plus

interest, attorney fees, costs, and other sums from the governmental body responsible for his loss, the Santa Monica Rent Control Board (the Board), in a complaint stating a cause of action in inverse condemnation. His complaint was dismissed. The Court of Appeal affirmed the trial court judgment and a majority of this court now affirms that judgment on the grounds that plaintiff's allegations, if true, do not establish a taking and, even if the Board's action denied him due process because it denied him a fair return on his property, he has another remedy--increased rents--by which means third parties may eventually reimburse him for what the Board allegedly took from him.

The majority err. There has been a taking of a substantial property right--plaintiff's right to seek a fair and reasonable return from his property. Plaintiff has both a federal and a state constitutional right to recover the loss he suffered as a result of that taking from the Board. By mandating rents so low that its action denied plaintiff due process of law, the Board took from him a significant stick in the bundle of sticks that together constitute ownership of real property (see Kaiser Aetna v. United States (1979) 444 U.S. 164, 176, 100 S. Ct. 383, 391, 62 L.Ed.2d 332)--the opportunity to earn a reasonable return on his property. Since the rent ceiling imposed by the Board denied plaintiff the reasonable return his property would otherwise have earned, it necessarily denied plaintiff economically productive use of his rental property and to that extent took a right to which he was constitutionally entitled. Under both the Fifth and Fourteenth Amendments to the United States Constitution (Fifth Amendment) and article I, section 19 of the California Constitution (article I, section 19), plaintiff must be compensated for that taking by the governmental entity that took his property. It is not sufficient that he is permitted to raise the rent paid by his tenants from which increases he may eventually recoup his losses.

I

THE "TAKINGS" CLAUSE AND RENT CONTROL

The Fifth Amendment taking clause, incorporated into and made applicable to the states by the Fourteenth Amendment (Chicago, Burlington & Q.R. Co. v. Chicago (1897) 166 U.S. 226, 239, 17 S.Ct. 581, 585-586, 41 L.Ed. 979), provides, inter alia that "private property [shall not] be taken for public use without just

compensation." Article I, section 19 contains a similar command, providing inter alia: "Private property may be taken or damaged for public use only *694 when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner." When the government fails to meet its constitutional obligation under these provisions, an action in inverse condemnation lies against the government to recover "just compensation." (Customer Co. v. City of Sacramento (1995) 10 Cal.4th 368, 377, fn. 4, 41 Cal.Rptr.2d 658, 895 P.2d 900.) And, even though the confiscatory rent ceiling imposed on plaintiff has been judicially invalidated, compensation must be paid for the income he lost while the impermissible rent ceiling was in effect, a period during which there was a "temporary taking." (First Lutheran Church v. Los Angeles County (1987) 482 U.S. 304, 321, 107 S.Ct. 2378, 2387, 96 L. Ed.2d 250.)

The Board may not avoid either a finding that there has been a taking or the obligation to pay constitutionally mandated compensation on speculation that plaintiff's loss may be reduced at some time in the future by increased rent paid by tenants who benefited from the reduced rent or, if those tenants leave, by new tenants who pay market rate rent. The question of whether there has been a taking must be decided independently of the value for just compensation purposes of any future monetary recovery from third parties allowed the owner whose property has been taken. (Suitum v. Tahoe Regional Planning Agency (1997) --- U.S. ----, 117 S.Ct. 1659, 137 L. Ed. 2d 980.)

The majority assume, but are reluctant to decide, whether a rent regulation which, as applied, denies a property owner due process constitutes a taking within the meaning of the Fifth Amendment and article I, section 19. I do not share that reluctance and I disagree with the view that there has been no taking in this case. I would hold that, because the rent regulation was adjudicated in Kavanau I to be so arbitrary as to deny due process by preventing plaintiff from earning a fair and reasonable return on the property, a taking occurred for which just compensation must be paid by the Board.

The interests which enjoy constitutional protection as "property" are generally defined by state law. (Civ.Code, § 755; Lucas v. South Carolina Coastal Council (1992) 505 U.S. 1003, 1030, 112 S.Ct. 2886, 2901, 120 L.Ed.2d 798.) In California "[t]he right to acquire

and possess property, guaranteed by the constitution, includes the right to dispose of it, or any part of it, and for that purpose to divide it in any possible manner, either by separating it into estates for successive periods or otherwise, and to dispose of one or more of such estates." (Tennant v. John Tennant Memorial Home (1914) 167 Cal. 570, 575, 140 P. 242; Gregory v. City of San Juan Capistrano (1983) 142 Cal.App.3d 72, 88, 191 Cal.Rptr. 47.) Just as that right encompasses the power to grant a license to use a portion of the owner's property temporarily (see Ex Parte Quarg (1906) 149 Cal. 79, 84 P. 766 [theater ticket]), it includes the right to create a leasehold estate.

Because the Board has not appropriated or physically invaded plaintiff's property, his claim is that there was a "regulatory taking," a restriction on his use of the property that went "too far" (Penna. Coal Co. v. Mahon (1922) 260 U.S. 393, 415, 43 S.Ct. 158, 160, 67 L.Ed. 322 (Pennsylvania Coal)), during the period for which he seeks damages. There was a "temporary taking." The contrary conclusion implicit in the majority opinion is foreclosed by the final judgment of the Court of Appeal in Kavanau I, supra, 19 Cal. App.4th 730, 23 Cal.Rptr.2d 724. The majority err both factually and legally therefore when they hold that there has been no taking because application of the Santa Monica rent control ordinance has not denied plaintiff " 'all economically beneficial or productive use of' his property." (Maj. opn., ante, at p. 684 of 66 Cal.Rptr.2d, p. 863 of 941 P.2d.) The Board did deny plaintiff all economically beneficial use of his property.

The legal conclusion that a taking occurred during the time that plaintiff was denied a fair and reasonable return on his rental property cannot be avoided under the United States Supreme Court precedent on which the majority rely. As the majority recognize, a regulatory taking may occur in a variety of contexts. The Supreme Court has identified many, implicitly concluding in some that because the governmental restriction went "too far," the property owner had been unfairly called upon to sacrifice a property *695 interest for the benefit of the public in circumstances in which the burden should be shared by the public as a whole. While the contexts in which the court has found a regulatory taking or rejected a taking claim differ, a common thread runs through the analysis. Although phrased somewhat differently in the court's various decisions, the economic

impact of the regulation on the property owner has been a determinative factor. When the regulation denies the owner economically productive use of the owner's property for its customary use, the regulation goes too far. It is irrelevant in those circumstances that the regulation furthers or is necessary to accomplish a legitimate public purpose that is otherwise within the police power of the government. A taking occurs for which just compensation must be paid.

"[W]hen the owner of real property has been called upon to sacrifice all economically beneficial uses in the name of the common good, that is, to leave his property economically idle" a taking occurs. (Lucas v. South Carolina Coastal Council, supra, 505 U.S. at p. 1019, 112 S.Ct. at p. 2895, fn. omitted.) The same is true if a regulation deprives the owner of economic use to the extent that the owner is unfairly singled out to bear a burden that should be borne by the public as a whole. (Yee v. Escondido (1992) 503 U.S. 519, 522-523, 112 S. Ct. 1522, 1526, 118 L.Ed.2d 153.) [FN1] A taking also occurs if a land use regulation extinguishes a fundamental attribute of ownership. (Agins v. Tiburon (1980) 447 U.S. 255, 262, 100 S.Ct. 2138, 2142, 65 L.Ed.2d 106; Kaiser Aetna v. United States, supra, 444 U.S. at pp. 179-180, 100 S.Ct. at pp. 392-393.)

FN1. The court noted in Yee that it had never considered whether a mobilehome rent control ordinance like that of the City of Escondido effected a regulatory taking, but refrained from addressing that issue only because the question has not been properly raised. (503 U.S. at p. 538, 112 S.Ct. at p. 1534.) The court expressed no doubt that a rent control ordinance could effect a regulatory taking. (Ibid., see also Pennell v. San Jose (1988) 485 U.S. 1, 108 S.Ct. 849, 99 L.Ed.2d 1.)

The taking clause necessarily applies to rent control ordinances which affect the ability of a property owner to earn a fair return on property which is generally used for rental purposes since the regulations restrict both the owner's fundamental right to create leasehold estates and the owner's right to make economically productive use of the property. The Fifth Amendment taking clause "is addressed to every sort of interest the citizen may possess" including leasehold interests. (U.S. v. General Motors Corp. (1945) 323 U.S. 373, 378, 65 S.Ct. 357, 359-360, 89 L.Ed. 311.) That the

Fifth Amendment taking clause applies to restrictions imposed by rent control ordinances has been acknowledged by the United States Supreme Court since at least 1921. In Block v. Hirsh (1921) 256 U.S. 135, 41 S.Ct. 458, 65 L.Ed. 865, the court upheld a rent control law applicable to the District of Columbia and made necessary by exigencies of the first World War. In so doing, the majority recognized that rent control regulations could be so restrictive as to amount to a taking. (Id. at p. 156, 41 S.Ct. at pp. 459-460.) In Bowles v. Willingham (1944) 321 U.S. 503, 518, 64 S.Ct. 641, 649, 88 L.Ed. 892, the court upheld a World War II price control act, some provisions of which applied to rental property, stating in reference to those provisions that "the restraints imposed on the national government in this regard by the Fifth Amendment are no greater than those imposed on the States by the Fourteenth."

The protection afforded by article I, section 19 is, of course, even broader than that of the Fifth Amendment. (Varjabedian v. City of Madera (1977) 20 Cal.3d 285, 298, 142 Cal. Rptr. 429, 572 P.2d 43.)

It is beyond dispute, therefore, that a rent control regulation that denies due process may also violate the taking clause of the Fifth Amendment, and article I, section 19. That being so, it is necessary to determine whether denying plaintiff the right to seek a fair return on his property did so. None of the decisions to which the majority look for identification of the factors relevant to determining whether a taking has occurred support the conclusion that no taking occurred here. It is clear to me that there has been a compensable taking.

In Pennsylvania Coal, supra, 260 U.S. 393, 43 S.Ct. 158, 67 L. Ed. 322, a seminal ***696** decision in the regulatory taking area, the Supreme Court considered the application of a Pennsylvania statute prohibiting anthracite coal mining in such a manner as to cause subsidence to a parcel of property. The property was subject to a deed executed by a coal company conveying the surface but expressly reserving the right to mine coal. The grantee of the surface interest expressly assumed all risk and waived all damage claims arising from the mining. The court held that application of the statute in these circumstances exceeded the police power of the state and constituted a compensable taking.

In reaching that conclusion the court recognized that property interests must yield "to some extent" to the police power, but this

implied limitation on the police power itself has limits imposed by the due process and contracts clauses of the Constitution. When exercise of the police power exceeds those limits, the government must exercise its power of eminent domain and pay just compensation. The "extent of the diminution" of the values incident to property determines when the limits of the police power have been exceeded. (Pennsylvania Coal, supra, 260 U.S. at p. 413, 43 S.Ct. at p. 159.) The coal company's reserved mining rights were recognized under Pennsylvania law, and therefore by the high court also, as a valuable estate in land. The extent of the taking was great, as application of the statute abolished that estate. (Id. at p. 414, 43 S.Ct. at pp. 159-160.)

In Pennsylvania Coal the court stated the general rule which continues to guide regulatory takings jurisprudence: "[W]hile property may be regulated to a certain extent, if regulation goes too far, it will be recognized as a taking.... [A] strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change." (Pennsylvania Coal, supra, 260 U.S. at pp. 415-416, 43 S. Ct. at p. 160.) [FN2]

FN2. The rule actually appears earlier in Block v. Hirsh, supra, 256 U.S. at page 56, 41 S. Ct. at pages 459-460, the decision in which the court held that rent control, including vacancy control, is not a per se taking. The law in question, applicable to Washington, D.C., property, provided procedures to assure the owner a reasonable rent. There, Justice Holmes explained that rent control is permissible when a public exigency makes that form of land use regulation necessary. Analogizing rent control to other permissible regulation of property he explained: "We do not perceive any reason for denying the justification held good in the foregoing cases to a law limiting the property rights now in question if the public exigency requires that. The reasons are of a different nature but they certainly are not less pressing.... All the elements of a public interest justifying some degree of public control are present. The only matter that seems to us open to debate is whether the statute goes too far. For just as there comes a point at which the police power ceases and leaves only that of eminent domain, it may be conceded that regulations of the

present sort pressed to a certain height might amount to a taking without due process of law." (Ibid., italics added.)

Subsequent decisions applying and further explicating that general rule make it clear that the property interest at issue here is a valuable right and that the manner in which the Board applied its rent control ordinance to plaintiff went "too far."

In Penn Central Transp. Co. v. City of New York (1978) 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631 (Penn Central), application of a landmark preservation law to plaintiff's property precluded a proposed development of the airspace above an historic railroad terminal building. The law did award transferable development rights to owners of landmark properties that could not be further developed. The court recognized that the availability of those rights was relevant in determining the economic impact of the regulation when deciding whether application of the law effected a taking. (See also Suitum v. Tahoe Regional Planning Agency, supra, --- U.S. ----, 117 S.Ct. 1659, 137 L.Ed.2d 980.) The question before the court was whether denying the owner the right to build above the existing landmark structure constituted a taking. The court again recognized that whether a taking has occurred depends on the circumstances of the individual case, and requires what is essentially an ad hoc, factual inquiry. It identified as a factor to be considered the "economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations." (*697 Penn Central, supra, 438 U.S. at p. 124, 98 S. Ct. at p. 2659.)

In applying its takings jurisprudence to Penn Central's property the court refused to consider the interest in airspace in isolation. It explained, "this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole--here, the city tax block designated as the 'landmark site.' " (Penn Central, supra, 438 U.S. at pp. 130-131, 98 S.Ct. at pp. 2662-2663.) After rejecting arguments that application of the landmark law to the property had diminished the value of the site and burdened Penn Central more than other property owners subject to it, noting that in these respects, the law was similar to a zoning ordinance, the court turned to the severity of the impact of the landmark law on the parcel as a whole. In concluding that the

impact was not such as to constitute a taking the court observed that the law did not interfere in any way with the existing use of the property, thus Penn Central's "primary expectation" about use of the parcel was unaffected. (Id. at p. 136, 98 S.Ct. at p. 2665.) It also noted that there had been no determination that all use of the airspace was prohibited since there had been no application for scaled-down development. Thus in this case, there had been no taking because "[t]he restrictions imposed are substantially related to the promotion of the general welfare and not only permit reasonable beneficial use of the landmark site but also afford appellants opportunities further to enhance not only the Terminal site proper but also other properties." (Id. at p. 138, 98 S. Ct. at p. 2666, fn. omitted, italics added.) The court emphasized that this holding assumed Penn Central's "present ability to use the Terminal for its intended purposes and in a gainful fashion." (Id. at p. 138, fn. 36, 98 S.Ct. at p. 2666, fn. 36.)

The importance of the right to use one's property in an economically viable manner as the determinative factor in assessing whether a taking has occurred was again emphasized by the court in Agins v. Tiburon, supra, 447 U.S. 255, 100 S.Ct. 2138, 65 L.Ed.2d 106. There the validity of zoning ordinances which limited the number of homes that could be constructed on a five-acre parcel was challenged. Because the property owners had not sought a development permit, the only question before the court was whether enactment of the ordinances alone constituted a taking. In rejecting the property owners' taking claim, the court stated: "The application of a general zoning law to particular property effects a taking if the ordinance does not substantially advance legitimate state interests, see Nectow v. Cambridge, 277 U.S. 183, 188 [48 S.Ct. 447, 448, 72 L.Ed. 842] (1928), or denies an owner economically viable use of his land, see Penn Central Transp. Co. v. New York City, 438 U.S. 104, 138, n. 36 [98 S.Ct. 2646, 2666, n. 36, 57 L.Ed.2d 631] (1978)." (Id. at p. 260, 100 S.Ct. at p. 2141, italics added.) Neither occurred as a result of the adoption of the Tiburon zoning ordinances. While they limited development, "they neither prevent[ed] the best use of appellants' land [citation], nor extinguish[ed] a fundamental attribute of ownership [citation]." (Id. at p. 262, 100 S. Ct. at p. 2142.)

Here, of course, the holding in Kavanau I, supra, 19 Cal.App. 4th 730, 23 Cal.Rptr.2d 724, establishes that plaintiff was not permitted

"economically viable" or "reasonably beneficial" use of his property. Application of the rent control ordinance to the property seriously interfered with his, or any owner of rental property's, "primary expectation" about the use of rental property, since the Board did not permit him to earn a reasonable rate of return. Moreover, by denying plaintiff that right, the Board effectively extinguished a fundamental attribute of ownership of rental property.

While the determination of whether a taking has occurred often does require weighing of private and public interests (Agins v. Tiburon, supra, 447 U.S. at p. 261, 100 S.Ct. at p. 2142), outside the realm of measures necessary to protect life and property (see, e.g., Miller v. Schoene (1928) 276 U.S. 272, 48 S.Ct. 246, 72 L. Ed. 568), the balance has never been struck in favor of public interest when governmental action has denied an owner economically viable use of the owner's property.

***698** The importance of the impact of governmental action on the profitability of property in the weighing process appears in Keystone Bituminous Coal Assn. v. DeBenedictis (1987) 480 U.S. 470, 107 S. Ct. 1232, 94 L.Ed.2d 472. There a state law, which required that 50 percent of extractable coal be left in place under specified structures to protect them against subsidence, was applied to property owned by the petitioners. The high court rejected a facial challenge to the law and distinguished Pennsylvania Coal, supra, 260 U.S. 393, 43 S.Ct. 158, on the ground that the petitioners had not shown that their mining operations were not profitable under the restrictions imposed by the law. "The two factors that the Court considered relevant have become integral parts of our takings analysis. We have held that land use regulation can effect a taking if it 'does not substantially advance legitimate states interest, ... or denies an owner economically viable use of his land.' Agins v. Tiburon, 447 U.S. 255, 260 [100 S.Ct. 2138, 2141, 65 L.Ed.2d 106] (1980) (citations omitted); see also Penn Central Transportation Co. v. City of New York, 438 U.S. 104, 124 [98 S.Ct. 2646, 2659, 57 L.Ed.2d 631] (1978).... [T]he character of the governmental action involved here leans heavily against finding a taking; the Commonwealth of Pennsylvania has acted to arrest what it perceives to be a significant threat to the common welfare. Second, there is no record in this case to support a finding ... that the Subsidence Act makes it impossible for petitioners to profitably engage in their business, or that there has

been undue interference with their investment-backed expectations." (Id. at p. 485, 107 S.Ct. at p. 1242.)

Under any of the high court's formulations of the test or factors relevant in assessing whether a regulatory taking has occurred, there has been a compensable taking in this case. When application of a rent control ordinance to a parcel of property is so arbitrary and unreasonable as to be confiscatory and deny due process, by definition that application has denied the owner all economically beneficial use of the property. When a rent ceiling is constitutionally impermissible because it denies a property owner a fair and reasonable return on the property, the owner's investment-backed expectations have been extinguished as the state has made use of the property "commercially impracticable," an action which constitutes a taking. (See Pennsylvania Coal, supra, 260 U.S. at pp. 414-415, 43 S.Ct. at pp. 159-160.) [FN3] The character of the government action is placement of the burden of assuring affordable rental housing, a burden that should be borne by the public as a whole, unfairly on the individual property owner. The owner is denied a reasonable return on his investment in order to benefit tenants. And, because the opportunity to lease property for an amount that will generate a reasonable return on the owner's investment is a fundamental aspect of property ownership, application of a rent control ordinance in a manner which denies the owner that opportunity extinguishes that incident of ownership.

FN3. An apartment building, unlike undeveloped land, is not amenable to a variety of uses or any alternative economically feasible use.

There can be no dispute over the fact that rent control is a taking for public use or common good. Rent control is constitutionally permissible precisely because it is perceived as a means by which the adverse impact on the public of a housing shortage may be cured or mitigated. (Birkenfeld v. City of Berkeley (1976) 17 Cal. 3d 129, 160, 130 Cal.Rptr. 465, 550 P.2d 1001.) "[A] primary purpose of rent control is the protection of tenants." (Pennell v. San Jose, supra, 485 U.S. at p. 13, 108 S.Ct. at p. 858.) It follows that when a rent ceiling is confiscatory the owner's right to use the property in an economically beneficial way "is being pressed into some form of public service under the guise of mitigating serious public harm."

(Lucas v. South Carolina Coastal Council, supra, 505 U.S. at p. 1018, 112 S.Ct. at p. 2895.)

Application of the additional factors identified by the majority (maj. opn., ante, at pp. 681-682 of 66 Cal.Rptr.2d, pp. 860-861 of 941 P.2d) as potentially relevant in determining whether a constitutional taking has occurred also leads ineluctably to the conclusion that there has been a taking in this case. The ***699** contrary reasoning of the majority is not supported by the authorities, discussed above, on which the majority rely. Those factors, in the order addressed by the majority, demonstrate the merit of plaintiff's claim:

1. The regulation of plaintiff's right to seek a reasonable return from his rental property does interfere with a property interest. Contrary to the majority view, the regulation did not simply delay the time at which plaintiff would receive the constitutionally adequate rents to which he was entitled. Application of the Santa Monica rent control ordinance by the Board has already denied plaintiff a fair return on his property. That temporary taking of this fundamental aspect of ownership allegedly cost plaintiff $113,095. Additionally, as his complaint alleges, the delay in receiving what would have been a fair return denied plaintiff the use of that money and interest of $30,956 that could have been earned.

Moreover, even assuming, as do the majority, that the government's obligation to pay just compensation may be shifted to third parties, there is no assurance that plaintiff will ever recoup his losses. It is true that he received some rental income, but that income was not a fair and reasonable return on the property. The complaint in inverse condemnation seeks to recover the rents that would have assured plaintiff a reasonable return, the amount taken from him by the Board's illegal application of the rent control ordinance.

2. The regulation did affect the existing use of plaintiff's rental property. It interfered to a constitutionally impermissible extent with his primary ownership expectation of receiving a reasonable return from rental property. Kavanau I, supra, 19 Cal.App.4th 730, 23 Cal.Rptr.2d 724, determined this.

3. It may be assumed that Santa Monica has a substantial interest in maintaining an adequate supply of affordable rental units, but that establishes only that the rent regulation is not invalid per se and that

plaintiff's property was taken for a public purpose. None of the authorities on which the majority rely suggest that this factor may ever outweigh the denial of an economically feasible use of property for its customary purpose in determining whether a taking has occurred.

4. The regulation did abrogate a substantial interest plaintiff holds in the property--the use of the property to produce a fair and reasonable return on plaintiff's investment. While he still owns the property, when rental property cannot be used to produce a fair and reasonable return, the only alternative to use of it for producing rental income is to sell it at a depressed price. Neither the Fifth Amendment nor article I, section 19 contemplates sale as an alternative economically feasible use. Both protect existing ownership interests.

5. The regulation has taken plaintiff's property to serve a public purpose.

6. It is given that the regulation did not permit plaintiff to earn a reasonable return.

7. Unlike Suitum v. Tahoe Regional Planning Agency, supra, --- U.S. ----, 117 S.Ct. 1659, 137 L.Ed.2d 980, and Penn Central, supra, 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631, which involved use restrictions, here the value of offsetting benefits such as the possibility that future increased rents permitted by the Board will offset some of plaintiff's losses is relevant only to whether just compensation has been paid. The existence of that possibility does not negate the fact that a taking has already occurred.

8. As applied in the past to plaintiff's property, the regulation did prevent the best and only economically feasible use of plaintiff's property, i.e., use to produce a reasonable income from rentals.

9. The regulation did extinguish a fundamental attribute of ownership--again the opportunity to rent or lease the property for rents that produce a fair and reasonable return during the period for which damages are sought. [FN4]

FN4. The tenth factor identified by the majority--permit-related requirements--is not involved here.

I agree therefore with Justice Mosk, who, in his dissenting opinion in Pennell v. City of *700 San Jose (1986) 42 Cal.3d 365, 376-377,

228 Cal.Rptr. 726, 721 P.2d 1111, expressed the view that a rent control ordinance which did not permit landlords with "hardship tenants" the same rental increases otherwise allowable, denied those owners a reasonable return on the property and thereby imposed on the owner what should be a public burden. The ordinance, he reasoned, created "forced subsidy imposed on the landlord in violation of the due process clauses of the United States and California Constitutions, which prohibit the taking of property without just compensation." (Id. at p. 377, 228 Cal.Rptr. 726, 721 P.2d 1111.)

II

THE RENTAL INCREASE ALTERNATIVE
TO AN INVERSE CONDEMNATION REMEDY

The majority apparently assume that plaintiff's rental units are and will continue to be occupied by some tenants who enjoyed the benefit of past impermissibly low rents. Therefore, the majority reason, we may justify compelling those tenants to pay rents which exceed the amount necessary to ensure plaintiff a reasonable return in order to reimburse plaintiff for what the government took. [FN5] Additionally, new tenants who pay market rate rents will help to reimburse him since those rents also exceed the amount necessary to ensure a reasonable return. Because plaintiff may recover his losses in this manner, there has been no taking and there is no need for an inverse condemnation remedy. Again, I disagree.

FN5. This assumption assumes in turn that rental increases sufficient to offset plaintiff's loss are permissible under Civil Code sections 1954.50 through 1954.53, the Costa-Hawkins Rental Housing Act which, while abrogating local limits on rent increases for vacant rental units, also contains a transitional limit for vacancies in rent controlled units of 15 percent more than the prior rental rate or 70 percent of the prevailing market rent. (Civ.Code, § 1954.53, subd. (c).)

The taking has already occurred. Plaintiff has already lost almost $150,000 because of the Board's action. Both the Fifth Amendment and article I, section 19 impose the obligation to pay just compensation on the governmental entity that takes an owner's property. Moreover, assuming either (1) that the availability of rent

increases might create a benefit adequate to permit a conclusion that there has been no taking, or (2) that the obligation to pay just compensation for a taking may be satisfied by shifting the burden to tenants through extraordinary rental increases, there is no assurance here that any present tenants on whom those increases fall will remain and pay the authorized increases. The majority's assumption that they will do so is unfounded. Also unfounded is the assumption that because plaintiff is allowed to raise the rent for vacant units, he will be able to recover his past losses from new tenants. The higher, presumably market rate, rents paid by new tenants are those which plaintiff would receive in any event since vacant units are no longer subject to rent control except to the extent that the preemptive state law imposes transitional limits. By no stretch of the legal imagination do these higher rents include a premium that will reimburse plaintiff for the past rental income which the Board wrongfully denied him. [FN6]

> FN6. It might be argued that because market rate rents in a tight rental market exceed a fair return on investment, the amount of that difference balances the losses suffered by an owner of rent regulated rental property when rents are set too low--i.e., the overall return meets the fair and reasonable return criterion. It does not follow, however, that receipt of market rate rental income to which the owner is entitled when a vacancy occurs, may be treated as compensation for past losses. Income which would be received in any case does not replace lost income.

Thus, the majority's holding that increasing the rents allowed for plaintiff's rental units is an adequate alternative to an action in inverse condemnation, rests entirely on speculation that plaintiff will someday recover the amount he allegedly lost from past tenants who will remain tenants even though the permitted rent increases will of necessity fix their rents at a figure above that otherwise permitted. It should be apparent to all that this illusory alternative remedy will not and cannot be considered an offsetting benefit that mitigates plaintiff's loss and relieves the Board of its obligation to pay for taking *701 plaintiff's property. The increased rents "remedy" neither precludes a finding that there has been a taking nor satisfies the constitutional command that just compensation be paid when a taking occurs.

The judgment dismissing plaintiff's cause of action for inverse condemnation should be set aside. For that reason, I would reverse the judgment of the Court of Appeal.

BROWN, J., concurs.

Filed 1/9/96

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION THREE

EARL W. KAVANAU, Plaintiff and Appellant, v. SANTA MONICA RENT CONTROL BOARD, an Agency of the City of Santa Monica, Defendant and Respondent.	)	B087620 (Super. Ct. No. BC 103933)

APPEAL from an order of the Superior Court of Los Angeles County.

Ricardo A. Torres, Judge. Affirmed.

Earl W. Kavanau, in pro. per., for Plaintiff and Appellant.

Anthony A. Trendacosta and Ralph H. Goldsen, for Defendant and Respondent.

INTRODUCTION

A property owner may seek money damages for a partial taking in the period during which the owner challenges the validity of a regulation. The property owner, however, must show that the regulation constitutes a "taking" by depriving the owner of all viable economic use of the property. Although a rent control statute as applied to plaintiff invalidly subjected rent increases to a 12 percent annual cap, during the period plaintiff challenged that regulation he continued to receive rent and retained many other economic uses of

his property. No taking occurred, and we affirm the sustaining of a demurrer to his inverse condemnation action.

On May 2, 1994, Earl W. Kavanau ("plaintiff" or "Kavanau") filed a complaint against the Santa Monica Rent Control Board ("defendant" or "the Board") alleging causes of action for inverse condemnation and for deprivation of civil rights (42 U.S.C. § 1983). The trial court sustained the Board's demurrer without leave to amend as to both causes of action. An order of dismissal was filed September 8, 1994.

Kavanau filed a notice of appeal on September 29, 1994.

STANDARD OF REVIEW

In reviewing the sufficiency of a complaint against a general demurrer, this court treats the demurrer as admitting all material facts properly pleaded, but not contentions, deductions, or conclusions of fact or law. This court also considers matters that may be judicially noticed. When a demurrer is sustained, this court determines whether the complaint states facts sufficient to constitute a cause of action. When a demurrer is sustained without leave to amend, this court decides whether a reasonable possibility exists that amendment may cure the defect; if it can we reverse, but if not we affirm. (*Blank v. Kirwan* (1985) 39 Cal.3d 311, 318.)

FACTS

The complaint contained the following allegations. Kavanau owns a 10-unit apartment building at 818 5th Street in Santa Monica, which is subject to the rent control law of the City of Santa Monica, which the Board administers.

Between November 1, 1988, and October 31, 1989, Kavanau collected $43,444 in rent and spent $160,499 operating, maintaining and improving the property. On November 30, 1989, Kavanau applied to the Board for rent increases on 9 of the 10 units pursuant to regulations governing rent-increase petitions and the Board's Maintenance of Net Operating Income ("MNOI") formula.

Although finding that Kavanau was entitled to immediate yearly rent increases of approximately $35,000, the hearing examiner allowed Kavanau to implement only $5,184 of that increase in the first year, with the balance of the $35,000 to be implemented over

eight years of annualized increases, each not to exceed a 12 percent cap.

Kavanau unsuccessfully appealed the hearing examiner's decision to the Board. The superior court denied his petition for a writ of administrative mandamus. Division One of this court reversed the superior court's ruling and held that the Board's regulation 4107 was unconstitutional as applied and directed the trial court to issue a writ of mandate commanding the Board to permit Kavanau to implement the remaining increases determined by the hearing examiner to be appropriate under the MNOI formula, without any reduction under Regulation 4107(a). (*Kavanau v. Santa Monica Rent Control Bd.* (1993) 19 Cal.App.4th 730, 736-737.)

As of the filing of the complaint, the Board's action caused Kavanau to lose rental income totaling $113,095: $34,729 (May 1990 to April 1991); $32,936 (May 1991 to April 1992); $26,410 (May 1992 to April 1993); and $19,020 (May 1993 to April 1994).

As a result of the Board's unlawful application of regulation 4107, Kavanau suffered a "taking" and "damaging" of his property rights pursuant to the California Constitution, article I, section 19, Code of Civil Procedure section 1036, and the United States Constitution. Kavanau lost monthly rental income beginning with the Board's May 1990 affirmance of the hearing examiner through the Board's April 14, 1994, compliance with the writ of mandate. The Board has deprived Kavanau of his federal and state constitutional rights to earn a fair return on his investment and of interest he could otherwise have earned, valued at approximately $30,956.

On appeal, Kavanau has abandoned his second cause of action for violation of civil rights.

ISSUES

Plaintiff claims on appeal that:

1. The failure to allow a landlord to earn a fair return is a "taking or damaging" pursuant to Califonia Constitution, article I, section 19; and that

2. He has suffered a state and a federal taking.

DISCUSSION

The complaint concerns the period between the Board's May 1990 affirmance of the hearing examiner's April 7, 1990, decision[1] and the Board's compliance with the writ of mandate on April 14, 1994. The complaint alleged damages beginning in April 1990 and ending in April 1994.

During this period, the hearing examiner found that under the MNOI formula, Kavanau was entitled to rent increases averaging approximately $323 per month per unit, or roughly $35,000 annually. The 12 percent cap limited those rent increases to $5,184. (*Kavanau, supra,* at pp. 733-734.)

Kavanau seeks recovery of rent increases retroactively from the Board, based on inverse condemnation.

a. *Inverse Condemnation*

The question in this appeal is whether a regulatory scheme which has been declared invalid, as applied to Kavanau, makes the Board liable to Kavanau for damages during the period the regulation was applied to his property.

Kavanau argues that the complaint states a cause of action based on article I, section 19 of the California constitution.[2] He argues that the Board should compensate him for the loss of $113,095 in rental income.

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[1] A date taken from *Kavanau v. Santa Monica Rent Control Bd., supra*, 19 Cal.App.4th at p. 734; the complaint alleges that the Board affirmed the hearing examiner's decision in May 1990.

[2] Article I, section 19 states: "Private property may be taken or damaged for public use only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner. The Legislature may provide for possession by the comdemnor following commencement of eminent domain proceedings upon deposit in court and prompt release to the owner of money determined by the court to be the probable amount of just compensation."

First Lutheran Church v. Los Angeles County (1987) 482 U.S. 304, 321 held that a landowner may bring an inverse condemnation suit based on a temporary regulatory taking, but only if the landowner had been denied all use of his property during the temporary taking. The court stated: "where the government's activities have already worked a taking of *all use* of property, no subsequent action by the government can relieve it of the duty to provide compensation for the period during which the taking was effective." (Emphasis added.) The case was remanded to the trial court to determine if the landowner had been denied *all* use of its land. On remand, *First English Evangelical Lutheran Church v. County of Los Angeles* (1989) 210 Cal.App.3d 1353, 1356 found, in part, that no taking occurred because the county ordinance in question advanced a preeminent state interest in public safety and did not deny the landowner all use of its property. The facts underlying the *First English* cases are important to their results.

The First English Evangelical Lutheran Church owned a parcel of flat land in a national forest sited next to Mill Creek, a drainage channel for an upstream watershed area owned by the National Forest Service. 3,860 acres of watershed burned in July 1977, creating a flood hazard. The following winter, a storm dropped 11 inches of water into the watershed, creating a wall of water and debris that swept away bridges and buildings, drowned 10 people, and caused millions of dollars in losses, including destruction of numerous buildings on the church's property. A county ordinance adopted after the flood prohibited reconstruction of buildings in the Mill Creek Canyon interim flood protection area, which included those flat areas of the church's property where its buildings formerly stood. (*Id.* at pp. 1356-1357; *First Lutheran Church v. Los Angeles County, supra,* 482 U.S. at p. 307.)

The trial court sustained a motion to strike that portion of plaintiff church's inverse condemnation action based on the taking of all use of church property by the county ordinance. The California Court of Appeal concluded that because the United States Supreme Court had not ruled on whether a state may limit the remedy for a taking to non-monetary relief, it was bound to follow *Agins v. Tiburon* (1979) 24 Cal.3d 266. *Agins* held that a property owner was not entitled to monetary damages until a court ruled a land use regulation was excessive and the government nevertheless chose to continue the

regulation in effect. (*First English Evangelical Lutheran Church v. County of Los Angeles, supra,* 210 Cal.App.3d at pp. 1358-1359.)

The United States Supreme Court, however, held that when an ordinance deprived a landowner of all use of its property for a considerable period, invalidating the ordinance without payment of fair value for the use of the property while the ordinance remained in effect would not be a constitutionally sufficient remedy. (*First Lutheran Church, supra,* at p. 322.) Even though it approved monetary damages for a "temporary regulatory taking," the United States Supreme Court remanded for a finding on whether such a taking had occurred.

On remand, the California Court of Appeal concluded that the case was not even close, and affirmed dismissal of the inverse condemnation action. (*Id.* at pp. 1361, 1374.) *First English Evangelical Lutheran Church v. County of Los Angeles* analyzed the issue as follows. The church operated the property as a camping facility. The ordinance prohibited reconstruction of structures demolished or damaged by floodwaters, and prohibited construction of new structures. But it did not prevent occupancy and use of structures that survived the flood; did not prohibit uses of the campground property which could be carried out without reconstructing old buildings or building new ones; and did not prohibit "uses of value to [the] purpose" of camping: "Meals could be cooked, games played, lessons given, tents pitched." *First English Evangelical Lutheran Church* concluded that the ordinance did not deny the church "all use" of its campground property, and this conclusion supported its holding that the complaint did not state a valid claim for a compensable taking. (*First English Evangelical Lutheran Church, supra,* 210 Cal.App.3d at pp. 1367, 1372.)

A taking occurs if, in applying a general regulation to particular property, the regulation "does not substantially advance legitimate state interests, [citation], or denies an owner economically viable use of his land, [citation]." (*Agins v. Tiburon* (1980) 447 U.S. 255, 260; *Lucas v. South Carolina Coastal Council* (1992) 505 U.S. 1003, __, [112 S. Ct. 2886, 2893].) Kavanau's eminent domain cause of action alleges the rent control statute deprived him of the economically viable use of his land for the period during which he litigated the rent control issue.

Kavanau v. Santa Monica Rent Control Board, supra, 19 Cal. App.4th 730, did not decide the eminent domain "taking" issue. Ruling instead on due process grounds, *Kavanau* held that the Santa Monica rent control statute was not *facially* invalid, but *as applied* to Kavanau it was unconstitutional because it did not meet the standard in *Cotati Alliance for Better Housing v. City of Cotati* (1983) 148 Cal.App.3d 280, 296: "The purpose of rent control is to permit an efficient landlord to pay all actual and reasonable expenses and receive a fair profit while, at the same time, protecting the public interest in having affordable and properly maintained rental housing available to the citizens of the community." *Cotati Alliance* is based on the due process standard of "just and reasonable return on [landlord's] property" in *Birkenfeld v. City of Berkeley* (1976) 17 Cal. 3d 129.[3] (*Cotati Alliance for Better Housing, supra,* at p. 293.)

"[W]hen the owner of real property has been called upon to sacrifice *all* economically beneficial uses in the name of the common good, that is, to leave his property economically idle, he has suffered a taking." (*Lucas v. South Carolina Coastal Council, supra,* 505 U.S. at p. ____ [112 S. Ct. at p. 2895]; italics in original.) As many cases illustrate, however, no inverse condemnation cause of action exists where there has not been a total "taking" of the landowners' property.

In *Guinnane v. City and County of San Francisco* (1987) 197 Cal. App.3d 862, 868, the plaintiff retained his right to exclude others from his land and to sell the property. No taking arose from defendant City's delay in granting plaintiff's application for a permit to build four houses on adjoining lots pending environmental review.

Gherini v. California Coastal Com. (1988) 204 Cal.App.3d 699, 713-714, found no compensable taking occurred because of the

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[3] Rent control provisions come within the police power if they are reasonably calculated to eliminate excessive rents and at the same time provide landlords with a just and reasonable return on their property. (*Birkenfeld, supra,* 17 Cal.3d at p. 165.) The constitution does not mandate a fair return on the value of a landlord's property, only a fair return on investment. (*Apartment Assn. of Greater L.A. v. Santa Monica Rent Control Bd.* (1994) 24 Cal.App.4th 1730, 1737; *Nash v. City of Santa Monica* (1984) 37 Cal.3d 97, 102.)

Coastal Commission's refusal to certify a proposed county land use plan and recommendations for revisions which did not deprive landowners of all economic use of their property insofar as it permitted 21 dwelling units on the owner's 6,700-acre parcel.

Smith v. City and County of San Francisco (1990) 225 Cal.App.3d 38, 45-46, found no deprivation of substantially all value arising from City's requiring an environmental impact report and temporary designation of three lots as open space in the general plan; landowners obtained an option to sell land, including the three lots, for $810,000, indicating that the lots retained significant value. A dispute over lot description and set-back requirements on lots large enough for development does not constitute a deprivation of substantially all use of property.

Terminals Equipment Co. v. City and County of San Francisco (1990) 221 Cal.App.3d 234, 242-244, found no inverse condemnation cause of action where landowners were not permitted to demolish a commercial building and build a larger, taller multipurpose office building, but were able to and did continue to use existing buildings on their property as they had for more than 40 years.

HFH, Ltd. v. Superior Court (1975) 15 Cal.3d 508, 514 held that inverse condemnation does not lie in zoning actions in which the complaint alleges a mere reduction in market value.

In *Terminal Plaza Corp. v. City and County of San Francisco* (1986) 177 Cal.App.3d 892, 912 the city enacted an ordinance restricting conversion of "residential hotels." The ordinance required owners of residential hotel units to obtain a permit before converting property to any other use and required property owners to build or rehabilitate an equal number of replacement units, or to contribute an "in lieu" fee, before a permit to convert property would be granted. *Terminal Plaza Corp.* found that the ordinance left the property owner with the right to sell or trade the property, to use the property in the same manner as before the ordinance, and to convert the property to other use upon compliance with the ordinance, and held that despite being restrictive and having the effect of reducing the value of the regulated properties, no taking occurred.

In *Pan Pacific Properties, Inc. v. County of Santa Cruz* (1978) 81 Cal.App.3d 244, 255-256, an ordinance allowed a one-family dwelling of an owner, employee or lessee on land zoned for agricultural use. This reclassified the land from commercial to agricultural use and thus diminished its value, but did not deprive the owners of all reasonable and beneficial use. *Sierra Terreno v. Tahoe Regional Planning Agency* (1978) 79 Cal.App.3d 439, 442-443, and *Pinheiro v. County of Marin* (1976) 60 Cal.App.3d 323, 328-329, are similar cases.

As stated in *Long Beach Equities, Inc. v. County of Ventura* (1991) 231 Cal.App.3d 1016, 1036, the denial of the highest and best use does not constitute an unconstitutional taking of property. Even where the government regulation diminishes the value of property very substantially, there is no taking. (*Ibid.*, citing *Hadacheck v. Sebastian* (1915) 239 U.S. 394: diminution in value from $800,000 to $60,000 not a taking; and *William C. Haas v. City & City. of San Francisco* (9th Cir. 1979) 605 F.2d 1117, 1120: diminution from $2 million to $100,000 not a taking.) *Long Beach Equities* also cited *MacLeod v. Santa Clara County* (9th Cir. 1984) 749 F.2d 541, 547 which found that a county's denial of a permit to harvest timber did not interfere with holding property for investment and with using the property for its original use, cattle grazing.

During the period in which he sought to invalidate its application to his property, Kavanau continued to receive rental income, even though it amounted to considerably less than the amount he would receive after *Kavanau* invalidated the 12 percent annual cap. Despite the application of the Santa Monica Rent Control law, moreover, numerous beneficial and substantial uses of the property remained. Kavanau could borrow against the property; refinance it; hold it for investment and appreciation; enjoy depreciation and other tax benefits; convert the property to condominiums (*City of West Hollywood v. Beverly Towers, Inc.* (1991) 52 Cal.3d 1184, 1188-1189); cease to do business as a landlord (Gov. Code § 7060, et seq.; *Javidzad v. City of Santa Monica* (1988) 204 Cal.App.3d 524); or sell the property.

We conclude that no compensable taking occurred, that the complaint does not state a cause of action for inverse condemnation, and that the trial court correctly sustained the demurrer. Kavanau has

not specified that there is a reasonable possibility he can amend his complaint to cure its defects. (*Careau & Co. v. Security Pacific Business Credit, Inc.* (1990) 222 Cal.App.3d 1371, 1386.) We therefore affirm the order of dismissal.

DISPOSITION

The order of dismissal is affirmed. Parties to bear their own costs on appeal.

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS.

KITCHING, J.

I concur:

KLEIN, P.J.

I respectfully dissent.

In the prior appeal (*Kavanau v. Santa Monica Rent Control Board* (1993) 19 Cal.App.4th 730), the court held that a portion of Santa Monica's rental control law (relating to the manner in which landlords could obtain a rent increase) was unconstitutional *as applied* to Kavanau. The reason for that conclusion was that the relevant regulations, as interpreted and applied by the Rent Control Board, did not permit Kavanau to receive a fair and reasonable return on his investment. A fair and reasonable return on investment standard is constitutional as applied only if the relevant regulation affords the administrative agency sufficient flexibility to avoid confiscatory results. (*Fisher v. City of Berkeley* (1984) 37 Cal.3d 644, 682; *Calfarm Ins. Co. v. Deukemejian* (1989) 48 Cal.3d 805, 816.) The regulations, as applied to Kavanau's rent increase applications, were found by the appellate court to be unconstitutionally confiscatory and the trial court was ordered to enter judgment in his favor and to issue a writ of mandate directing

the Board to permit Kavanau to impose the rental increases found to be due.

In this action, we are bound by that determination. Thus, I would phrase the issue raised somewhat differently from my colleagues. The question presented by this case is whether the actions of the Board in depriving Kavanau of rental increases to which he was *constitutionally* entitled, during the period May 1990 through April 1994, constituted a compensable taking so as to enable him to maintain an action for inverse condemnation. This is no small matter. The impact on Kavanau was substantial. He alleges that $113,095 in rental income (plus over $30,000 in lost interest on such funds) was effectively transferred from him to his tenants by the Board's unconstitutional conduct. If he is not able to recover this sum from the defendant City, then from whom? If the theory of such recovery is not inverse condemnation, then what?[4]

The Fifth Amendment to the United States Constitution, made applicable to the several states through the Fourteenth Amendment (*Chicago, B. & Q. R. Co. v. Chicago* (1897) 166 U.S. 226, 239), provides that "private property [shall not] be taken for public use, without just compensation." It is well settled that the purpose of this provision is "to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." (*Armstrong v. United States* (1960) 364 U.S. 40, 49; see also *Agins v. Tiburon* (1980) 447 U.S. 255, 260-263; *First English Evangelical Lutheran Church of Glendale v. Los Angeles County* (1987) 482 U.S. 304, 318-319; *Nollan v. California Coastal Commission* (1987) 483 U.S. 825, 835-836, fn. 4.)

Conceptually, there are three categories of potential takings: (1) outright physical taking (e.g., flooding, destruction or physical

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[4] "An action in inverse condemnation arises directly from the constitutional provision (art. I, § 19) and is independent of any right to sue under traditional tort theories. [Citations.] The right to sue in inverse condemnation is 'fundamentally rooted' in the Constitution, and the extent of a public entity's liability is fixed by the Constitution and not by rules of statutory or common law rights and responsibilities between private parties. [Citation.]" (*Rose v. City of Coalinga* (1987) 190 Cal.App.3d 1627, 1635.)

occupation by government), (2) physical taking by regulation (e.g., regulatory measures authorizing permanent physical use of property by third parties), and (3) pure regulatory takings (i.e., regulations prohibiting or requiring certain uses of property by its owner). The first two categories require compensation (*Loretto v. Teleprompter Manhattan CATV Corp.* (1982) 458 U.S. 419, 426.) The third may or may not constitute a compensable taking depending on the facts and circumstances.

As Justice Holmes stated over 70 years ago, "[w]hile property may be regulated to a certain extent, if regulation goes *too far* it will be recognized as a taking" (*Pennsylvania Coal Co. v. Mahon* (1922) 260 U.S. 393, 415; italics added.) Unfortunately, Justice Holmes did not define what was meant by the term "too far." As already noted, the Supreme Court in 1960, held that a governmental action will constitute a regulatory taking if it goes so far as to unfairly single out a property owner to bear a burden which society should bear as a whole. (*Armstrong v. United States, supra,* 364 U.S. at p. 49.) In 1978, in *Pennsylvania Central Transportation Company v. New York City* (1978) 438 U.S. 104, 125, the court identified five factors which must be considered when determining whether the regulation has gone so far as to require compensation: (1) the economic impact of the regulation on the owner, (2) the extent of the interference with the owner's reasonable investment-backed expectations, (3) the character and nature of the regulation, (4) the extent to which the owner benefits from the regulation, and (5) the nature and importance of the public interests which the regulation serves.

Unfortunately, the *Pennsylvania Central* court did not define the terms used in these general guidelines. However, this rather vaguely expressed concern with the nature and impact of regulation was refined and elevated to a two-part threshold inquiry in *Nollan v. California Coastal Commission, supra,* 483 U.S. 825. Borrowing language from *Agins v. Tiberon, supra,* 447 U.S. 255, the *Nollan* court held that land use regulations will require compensation under the Takings Clause if (1) they fail to "substantially advance legitimate state interests" *or* (2) they deny an owner an "economically

viable use." (*Nollan, supra*, 483 U.S. at p. 834.)[5] " '[A] use restriction may constitute a taking if not reasonably necessary to the effectuation of a substantial government purpose.' " (*Id* at p. 834, quoting from *Pennsylvania Central, supra,* at p. 127.)

Our own Supreme Court recently summarized these rules in *Hensler v. City of Glendale* (1994) 8 Cal.4th 1. " 'Where the government authorizes a physical occupation of property (or actually takes title), the Takings Clause generally requires compensation. [Citation.] But where the government merely regulates the use of property, compensation is required only if considerations such as the purpose of the regulation or the extent to which it deprives the owner of the economic use of the property suggest that the regulation has unfairly singled out the property owner to bear a burden that should be borne by the public as a whole.' [Citation.] An individualized assessment of the impact of the regulation on a particular parcel of property and its relation to a legitimate state interest is necessary in determining whether a regulatory restriction on property use constitutes a compensable taking. [Citation.]" (*Id.* at pp. 9-10.)

A rent control ordinance is a proper exercise of local government's police power if it is "reasonably calculated to eliminate excessive rents and at the same time provide landlords with a *just and reasonable return on their property*." (*Birkenfeld v. City of Berkeley*

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[5] In 1994, in *Dolan v. City of Tigard* (1994) _ U.S. _ [129 L. Ed.2d 304, 114 S.Ct. 2309], the Supreme Court reached a related issue left open by *Nollan*. In a case involving conditions imposed upon a commercial property owner seeking to double the size of her retail store and pave over her parking lot, the court held that to avoid the conclusion that the building permit conditions did not involve a "taking," the City had to demonstrate not only (1) that an *essential nexus* existed between the legitimate state interests involved and the permit conditions (a requirement imposed by *Nollan*), but also (2) that there was a *rough proportionality* between the exactions and the projected impact of the proposed development. (129 L. Ed.2d at p. 317.)

(1976) 17 Cal.3d 129, 165, italics in original.)[6] A rent control ordinance that failed to meet this standard would be unconstitutionally confiscatory; that is, it would deny due process. "[I]nherent in the *Birkenfeld* due process standard of 'a just and reasonable return on their property' is the assurance that an efficient landlord may recover all reasonable expenses actually incurred and, in addition, receive a fair profit or return on investment. [Citation.]" (*Cotati Alliance For Better Housing v. City of Cotati, supra,* 148 Cal. App.3d at p. 293.) The failure of a rental control ordinance to meet this standard "might well violate prohibitions against the taking of private property for public use without just compensation contained in the Fifth Amendment to the United States Constitution and article I, section 19 of the California Constitution." (*Id.* at p. 293; see also, *Searle v. City of Berkeley Rent Stabilization Bd.* (1988) 197 Cal. App.3d 1251, 1259.)

Where, as here, the rent control ordinance is unconstitutionally applied so as to deprive the landlord of a "just and reasonable return" on his investment, then under *Birkenfeld,* it would *not* be a proper exercise of the police power. If such *improper* exercise of power results in a deprivation of the landlord's property (e.g., his right to receive certain rentals, a concededly significant aspect of the ownership rights to income producing rental property), then how can it be denied that a taking has occurred. Would not such a governmental invasion clearly satisfy Justice Holmes' test in *Pennsylvania Coal, supra,* of going "too far"? Would not such a circumstance

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[6] Another California court described the legitimate purpose of a rent control law in these terms: "We emphasize that the purpose of rent control is not to make the landlord a private guarantor of affordable housing for tenants, nor is it to bring about such a degree of decreased maintenance and services as to diminish the quality of housing available. The purpose of rent control is to permit an efficient landlord to pay all actual and reasonable expenses and receive a fair profit while, at the same time, protecting the public interest in having affordable and properly maintained rental housing available to the citizens of the community." (*Cotati Alliance for Better Housing v. City of Cotati* (1983) 148 Cal.App.3d 280, 296.)

easily satisfy the general guidelines set out in *Pennsylvania Central*?[7] Finally, is there any way in which such an unconstitutional deprivation would not run afoul of both *Nollan* and *Dolan*? There is no legitimate state interest served by ignoring the due process rights of private citizens. To the contrary, any act of government which *unconstitutionally* interferes with the private property interests of its citizens must, perforce, result in a taking of property without just compensation to the extent that any uncompensated deprivation results.

In *Pennell v. San Jose* (1987) 485 U.S. 1, the Supreme Court did not reach the "takings" issue, although it was expressly raised and argued, because it was deemed "premature." However, Justice Scalia wrote in concurrence and dissent (joined by Justice O'Connor) that the addition by the City of San Jose of a "tenant hardship" factor in the regulatory processing of rental increase applications constituted a taking of the landlord's property without just compensation. (485 U.S. at pp. 19-24; conc. and disn. opn. of Scalia, J.) More significantly, in view of the majority's decision in this case that no taking could occur as a matter of law, both *Pennell, supra,* at pages 9-10 and *Yee v. Escondido* (1992) 503 U.S. _ [110 L.Ed.2d 153, 169] clearly recognized that a compensable taking could occur in the enforcement of a rent control regulation. Both cases had the issue presented but held that until a rent control regulation was unconstitutionally applied so as to deprive a landlord of a rental

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[7] In my view, each of the five factors set out in *Pennsylvania Central* would be implicated by government's unconstitutional imposition and enforcement of a confiscatory regulation. First, the economic impact on the landlord could range from serious to catastrophic, but it would always be significant because the government's actions were illegal. Second, for the same reason, the interference with the landlord's investment backed expectations would also be significant; imposition and continued enforcement of illegal regulations are never to be reasonably anticipated. Third, the character and nature of an illegal regulation which is nonetheless enforced will always be both odious and, by definition, unfairly burdensome. Fourth, the landlord obviously receives no benefit from the enforcement of an unconstitutional confiscatory regulation. Fifth, no public interest is ever served by government action in defiance of the Constitution.

which would have otherwise been permitted under a constitutional application of the regulation, then a taking claim was simply premature.

The relevant inference to be drawn from these cases, in the context of this case, is that, contrary to the views of the majority, a takings claim is indeed appropriate. The unconstitutional application, which was missing in both *Pennell* and *Yee*, is clearly present here. As we have already noted, that issue was finally resolved by the prior appellate decision.

The record in this case clearly shows that the defendant's unconstitutional acts resulted in the involuntary transfer of $113,095 of Kavanau's money to his tenants. The entire discussion by the majority, relying on a series of traditional land use regulation cases, is of little value to the precise issue presented here. Those cases simply deal with examples of governmental regulations which have not gone "too far," or, in the words of *Nollan*'s second prong, have not destroyed all economically viable usage of the property subject to the regulation. They have no relevance whatever to the facts of this case.

Moreover, the clear requirement of *Nollan* and *Dolan* that a regulation substantially advance the legitimate state interest sought to be achieved cannot be satisfied by showing that the State " 'could rationally have decided' the measure adopted might achieve the State's objective." (*Nollan v. California Coastal Commission, supra*, 483 U.S. at p. 834, fn. 3.) This is obviously stricter than the economic due process standard previously applied to non-physical takings. It has particular application to regulations controlling rents (none of the land use cases relied upon by the majority involve rent control). As one commentator concluded: "With the possible exception of a short-term response to a wartime emergency, the traditional objectives of rent control are highly vulnerable to attack under *Nollan*'s substantial advancement test. Responding to housing shortages or redistributing wealth may be regarded as legitimate state interests, but rent control generally fails to substantially advance these goals. Conversely, the political objectives that are furthered by rent control are of dubious legitimacy. . . . [¶] . . . The Supreme Court clearly demonstrated in *Nollan* that if a suspect regulation fails to substantially advance legitimate state interests, a taking will be

found regardless of the economic impact on the property owner. At the same time, however, the *Nollan* [c]ourt reiterated the second prong of its threshold inquiry under which a land use regulation violates the Takings Clause; namely, whether it denies the owner 'economically viable use' of property. Although it was not necessary to reach this test in *Nollan*, the [c]ourt has made it clear that deprivation of economically viable use by itself is sufficient evidence of a taking, regardless of the government interests served. [¶] This test, focusing on a challenged regulation's economic impact, is the lineal descendent of Justice Holmes' rule that if otherwise legitimate regulation 'goes too far' it will be recognized as a taking." (R.S. Radford, *Regulatory Takings Law in the 1990: The Death of Rent Control* (1992) 21 Sw. U. L.Rev. 1019, 1065; fns. omitted.)

With respect to the economically viable use test, upon which the majority entirely relies, and leaving aside for a moment the critical fact that the City's acts have already been determined to be unconstitutional, the application of that test will necessarily depend on how broadly the relevant property interest is defined. The more narrow the protected interest, the more easily a regulation may be found to deprive an owner of an economically viable use of that interest. The majority chooses to define Kavanau's property interest in the broadest possible terms. My colleagues emphasize that Kavanau still owned his apartment building, he could sell it, convert it to condominiums, borrow against it, receive (some) rental income from it and could continue to enjoy all of the related appreciation, depreciation and other tax benefits. I would argue, on the other hand, that it is more just and reasonable to define his property interest narrowly and limit it to the property actually taken from him; that is, the rentals which the defendant's own regulations entitled him to receive if they had been legally applied.

However, in my view, the most dispositive factor presented by this case is that we already have before us a final and binding judicial determination that the defendant's rent control regulations went "too far." As applied to Kavanau, those regulations have already been found to be confiscatory of his property (i.e., his right to receive a fair and reasonable return on his investment). I can perceive of no reason in law or logic why a confiscatory rent control regulation, found to be unconstitutional on due process grounds, would not result in a compensable taking if it were nevertheless enforced and a monetary

deprivation resulted. I can imagine no clearer example of a case where compensation should be paid than where the government has *illegally* taken or diverted to its own social goals the private property of one of its citizens. Indeed, such a common sense result and statement of principle should need no citation of authority.

I assume my colleagues would have no trouble perceiving a compensable "taking" of Kavanau's property had the City of Santa Monica seized $113,095 from his bank account in order to feed the City's homeless population. If that be so, why the difficulty here? The defendant's unconstitutional application of its own rent control regulations was no different and had the identical consequence. The government deprived Kavanau of his money to further its own social goals and has refused to compensate him. Such an unjust result cannot be defended on the ground that he has been left with the remaining portion of his property interests. If that is a justification for the defendant's illegal actions, then what was the purpose, consequence or meaning of the earlier determination that the defendant's regulations were unconstitutional as applied to Kavanau's rental property?

The demurrer to Kavanau's complaint should have been overruled. This is not a case which can be resolved against Kavanau on demurrer. I believe that he has alleged facts which demonstrate the existence of a claim for damages based upon the theory of inverse condemnation. I further believe those claimed damages arise from the defendant's wrongful taking of his property. Nor would it be proper to justify the majority's conclusions by reliance on the fact that Kavanau could have sought monetary relief in the prior action. While he was certainly free to join an inverse condemnation claim with his administrative mandamus action (*Hensler v. City of Glendale, supra,* 8 Cal.4th at p. 14), he was not required to do so. As we said in *Patrick Media Group, Inc. v. California Coastal Com.* (1992) 9 Cal.App.4th 592: "Special procedural requirements apply where an inverse condemnation action is based upon a regulatory taking accomplished by a discretionary action of an administrative agency. In such cases, the proper procedure is to bring the inverse condemnation action in conjunction with, *or after,* a petition for administrative mandamus, as defined in section 1094.5 of the Code of Civil Procedure, the procedure generally required when the validity or propriety of an action or determination by an

administrative agency is challenged. [Citations.]" (*Id.*, at p. 607, italics added.)

It is indeed unfortunate that my colleagues are willing to sanction a result which is not only unjust, but also involves an undisputed injury to a private citizen flowing from an unlawful act of government. Hopefully, the Supreme Court will accept the opportunity presented by this case to address what appears to be an important and novel issue: Will a government's unconstitutional imposition and enforcement of a confiscatory rent control regulation give rise to a private property owner's right to assert an inverse condemnation claim for a resulting monetary deprivation?

CROSKEY, J.

ANTHONY A. TRENDACOSTA, CSB 67840
General Counsel
RALPH H. GOLDSEN, CSB 96842
Staff Attorney
SANTA MONICA RENT CONTROL BOARD
1685 Main Street, Room 202
Santa Monica, California 90401
(310) 458-8781

Attorneys for Defendant
Santa Monica Rent Control Board

Filed 9/8/94
Dept. 64

IN THE SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF LOS ANGELES

EARL W. KAVANAU, Plaintiff, v. SANTA MONICA RENT CONTROL BOARD, an Agency of the City of Santa Monica, Defendant.	CASE NO. BC103933 ORDER OF DISMISSAL ~~[PROPOSED]~~

The demurrer of plaintiff Santa Monica Rent Control Board ("Board") came on regularly for hearing pursuant to noticed motion on August 11, 1994, in Department 64 of the above-entitled court. Earl W. Kavanau, plaintiff in propria persona, appeared on his own behalf. Ralph H. Goldsen, staff attorney, appeared on behalf of the Board. The court read and considered the complaint, the demurrer, plaintiff's opposition to the demurrer, and defendant's reply to the demurrer, and heard oral argument. The court thereupon sustained defandant's demurrer without leave to amend as to both causes of action. Good cause appearing therefrom,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that this action is dismissed with prejudice. Costs are not awarded in this proceeding.

DATED: Sep 08 1994.

By: /s/ Ricardo A. Torres
Hon. Ricardo A. Torres, Judge

Filed
Los Angeles Superior Court
Aug 12 1994
Edward M. Kritzman, Clerk

By P. Offord, Deputy

ANTHONY A. TRENDACOSTA, CSB 67840
General Counsel
RALPH GOLDSEN, CSB 96842
Staff Attorney
SANTA MONICA RENT CONTROL BOARD
1685 Main Street, Room 202
Santa Monica, California 90401
(310) 458-8781

Attorneys for Defendant
Santa Monica Rent Control Board

IN THE SUPERIOR COURT

OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF LOS ANGELES

EARL W. KAVANAU, Plaintiff, v. SANTA MONICA RENT CONTROL BOARD, an Agency of the City of Santa Monica, Defendant.	)	CASE NO. BC103933 **NOTICE OF RULING ON DEFENDANT'S DEMURRER TO COMPLAINT**

TO: EARL W. KAVANAU, plaintiff in propria persona:

PLEASE TAKE NOTICE that on August 11, 1994, in Department 64 of the Los Angeles County Superior Court, the Hon. Ricardo Torres, Judge Presiding, the demurrer of plaintiff Santa Monica Rent

Control Board ("Board") came on regularly for hearing pursuant to noticed motion. Earl W. Kavanau, plaintiff in propria persona, appeared on his own behalf. Ralph H. Goldsen, staff attorney, appeared on behalf of the Board. The court read and considered the complaint, the demurrer, plaintiff's opposition to the demurrer, and defendant's reply to the demurrer, and heard oral argument.

The court thereupon sustained defendant's demurrer without leave to amend as to the first cause of action for inverse condemnation on the first ground stated in the demurrer, namely that plaintiff had failed to allege and could not allege a deprivation of all economic use of his property, as required for a temporary taking claim under *First English Evangelical Lutheran Church v. County of Los Angeles* (1987) 482 U.S. 304, 96 L.Ed. 2d 250, 107 S.Ct. 2318.

The court sustained defendant's demurrer without leave to amend as to the second cause of action for violation of civil rights on the sixth ground stated in the demurrer, namely that such action accrued in 1990 and became barred by the statute of limitations in 1991, a year later.

The court directed defendant to give notice of its ruling. Defendant Board will prepare a proposed order of dismissal and submit it to the court after the passage of 10 days.

DATED: August 12, 1994

ANTHONY A.TRENDACOSTA
General Counsel

By: /S/ RALPH H. GOLDSEN
RALPH H. GOLDSEN
Staff Attorney

Attorneys for Defendant
SANTA MONICA RENT
CONTROL BOARD

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23 Cal.Rptr.2d 724, 19 Cal.App.4th 730, Kavanau v. Santa Monica Rent Control Bd., (Cal.App. 2 Dist. 1993)

*724 19 Cal.App.4th 730

Earl W. KAVANAU,

Plaintiff and Appellant,

v.

SANTA MONICA RENT CONTROL BOARD,

Defendant and Respondent.

No. B073052.

Court of Appeal, Second District, Division 1.

Oct. 21, 1993.
Rehearing Denied Nov. 9, 1993.
Review Denied Feb. 3, 1994.

[19 Cal.App.4th 731] Earl W. Kavanau, in pro. per.

Trevor Grimm, Los Angeles, and Craig Mordoh, Santa Monica, as amici curiae, on behalf of Apartment Ass'n of Los Angeles County, Inc.

Gilbert H. Friedman, Los Angeles, Anthony A. Trendacosta, Gen. Counsel, Ralph H. Goldsen, Staff Atty., for defendant and respondent.

*725 [19 Cal.App.4th 732] MIRIAM A. VOGEL, Associate Justice.

The issue in this case is whether the City of Santa Monica Rent Control Board's absolute limitation on annual rental increases is constitutional as applied.

Our answer is that it is not.

FACTS

A.

In 1979, the City of Santa Monica adopted a rent control charter amendment and created an elected Rent Control Board "empowered to regulate rentals ... so that rents will not be increased unreasonably and so that landlords will receive no more than a fair return." Pursuant to the charter amendment, the Board adopted Regulations 4100 through 4111, a "maintenance of net operating income" (MNOI) formula to determine whether a landlord is receiving a fair return and, if not, the basis on which rents can be increased. (FN1) The MNOI, in turn, is limited by Regulation 4107.

Under Regulation 4107(a), regardless of the amount of rent needed to satisfy the MNOI formula, and notwithstanding any other provision of the regulations, "[n]o upward rent adjustment may be authorized for any 12 month period in an amount in excess of twelve percent (12%) or twice the Employment Cost Index (ECI), whichever is greater." (We refer to this as a 12 percent cap.) If the amount of any adjustment otherwise authorized by the MNOI formula exceeds 12 percent, "the full justified amount shall be granted over a period of years such that the rent does not increase by greater than the said limit in any given year." Simply put, under Regulation 4107(a), rents can never be increased more than 12 percent (or twice the ECI) in any year, notwithstanding the amount of entitlement under the MNOI.

B.

In 1988, Earl W. Kavanau purchased a 10-unit apartment building in Santa Monica which was badly in need of repair. Between November 1, [19 Cal.App.4th 733] 1988, and October 31, 1989, Kavanau spent $98,099 on the building ($33,565 on operating expenses such as taxes, utilities and maintenance, plus $64,534 on capital improvements). (FN2) For the same period, his annualized debt service (which is excluded from the MNOI calculation) was $44,000. (Regulation 4101(c)(2)(ii) [mortgage principal and interest payments shall not be considered as an operating expense]; compare Cotati Alliance for Better Housing v. City of Cotati (1983) 148 Cal.App.3d 280, 294, 195 Cal.Rptr. 825 [to be fair and reasonable, the allowed amount of rent should permit the property to

generate income sufficient to cover the costs of operation and the servicing of reasonable financing and should ensure the return of a reasonable profit].) His annualized rental income for that period was $43,444. (FN3)

*726 In November 1989, Kavanau applied to the Board for permission to raise rents, seeking an average increase of about $474 per month for nine of the ten units. In April 1990, the Board's hearing examiner determined that Kavanau was entitled, under the MNOI, to permanent increases of $183 per month per unit, plus an additional $140 per month per unit for the duration of the useful life of the capital improvements, a total of $323 per month per unit, starting immediately. (These figures are approximate, as they vary from unit to unit and, for the sake of simplicity, we use the rough figure of $35,000 to refer to the increased rent Kavanau would receive for the year in question if he had the benefit of the hearing examiner's findings under the MNOI.) To state the obvious, the hearing examiner's findings necessarily included the determination that, without the allowed increase, Kavanau was not making a fair return on his investment.

By applying the 12 percent cap, however, the hearing examiner reduced Kavanau's first year rent increase from $35,000 to $5,184, with the balance of the $35,000 to be implemented over eight years of annualized increases, each not to exceed the 12 percent cap. (FN4) Although Kavanau offered evidence to show why, in his view, the 12 percent cap ought not to be applied to him, [19 Cal.App.4th 734] the hearing examiner ruled all such evidence irrelevant and inadmissible. On April 7, 1990, the hearing examiner issued his decision, with findings that Kavanau was entitled to a $35,000 increase under the MNOI formula. Kavanau's rental increases were nevertheless limited by the 12 percent cap, to a total of $5,184.

Kavanau appealed to the Board, without success, and he then petitioned the trial court for a writ of administrative mandate to overturn the Board's decision. While the matter was pending in the trial court, the Board added a new subdivision (f) to Regulation 4107, to authorize a waiver of the 12 percent cap "in extraordinary circumstances." Later, Kavanau's petition was denied and he appeals from the judgment thereafter entered. (FN5)

DISCUSSION

Kavanau contends Regulation 4107(a) is facially unconstitutional or, alternatively, unconstitutional as applied to his situation. For the following reasons, we agree that the regulation is unconstitutional as applied.

A.

First, we summarily reject the Board's rather disingenuous assertion that the constitutionality of Regulation 4107(a) was determined in Baker v. City of Santa Monica, supra, 181 Cal.App.3d at p. 988, 226 Cal.Rptr. 755. Baker holds only that net operating income standards (such as Santa Monica's) have been approved by our courts. Regulation 4107 is not discussed (it is not even mentioned).

B.

[1][2] Second, we recite the basic requirements of a valid rent control scheme: *727 Although no particular formula is required, the rules adopted must be reasonably calculated to eliminate excessive rents while at the same time providing "landlords with a just and reasonable return on their property." [19 Cal.App.4th 735] (Birkenfeld v. City of Berkeley, supra, 17 Cal.3d at p. 165, 130 Cal. Rptr. 465, 550 P.2d 1001; Fisher v. City of Berkeley, supra, 37 Cal.3d at pp. 680-681, 209 Cal.Rptr. 682, 693 P.2d 261.) The formula cannot be confiscatory (Calfarm Ins. Co. v. Deukmejian, supra, 48 Cal.3d at pp. 816-821, 258 Cal.Rptr. 161, 771 P.2d 1247) and it cannot impose an absolute limit on rental increases (id. at p. 817, 258 Cal. Rptr. 161, 771 P.2d 1247; City of Miami Beach v. Forte Towers, Inc. (Fla.1974) 305 So.2d 764; Cromwell Assocs. v. Newark, supra, 511 A.2d at p. 1275 [any absolute limit, "even a generous 25%," is arbitrary in that it may not insure a fair return in all circumstances].)

C.

[3][4] Third, we turn to Regulation 4107(f) (the Board's new authority to waive the 12 percent cap "in extraordinary circumstances") which, on its face, would appear to save the 12 percent cap from Kavanau's constitutional attack. Obviously, the 12 percent cap would not be an "absolute" limit if it could be waived

when required to permit a landlord a fair, just and reasonable return on his investment.

But that is not what the Board has in mind. At oral argument, we asked counsel for the Board to identify the type of circumstance which might be considered "extraordinary" within the meaning of Regulation 4107(f). Quite frankly, the answer we got was not the one we expected--as the Board intends to apply Regulation 4107(f), a landlord whose building is substantially destroyed by an earthquake and who has difficulty obtaining financing to rebuild it would "probably" be eligible for relief from the 12 percent cap. But a landlord in the position of Earl Kavanau would not. In short, to the City of Santa Monica's Rent Control Board, "extraordinary" means insolvency or an act of God is threatened or has actually arrived and it does not include the mere loss of a fair and reasonable return. (Cf. Calfarm Ins. Co. v. Deukmejian, supra, 48 Cal.3d at p. 818, 258 Cal. Rptr. 161, 771 P.2d 1247.) (FN6)

D.

With the addition of subdivision (f)'s "extraordinary circumstances" waiver of the 12 percent cap, Regulation 4107(a) is not unconstitutional on [19 Cal.App.4th 736] its face. (Fisher v. City of Berkeley, supra, 37 Cal.3d at p. 679, 209 Cal.Rptr. 682, 693 P.2d 261 [a regulation will be declared invalid on its face only when its terms do not permit those who administer it to avoid confiscatory results in its application].) But with the Board's interpretation of subdivision (f), section 4107(a) is unconstitutional as applied in this case. (Id. at p. 682, 209 Cal.Rptr. 682, 693 P.2d 261 [a fair return on investment standard is constitutional as applied only if the regulation affords the Board sufficient flexibility to avoid confiscatory results]; Calfarm Ins. Co. v. Deukmejian, supra, 48 Cal.3d at p. 816, 258 Cal. Rptr. 161, 771 P.2d 1247 [we focus less on the rate specified in the regulation than on the ability of the person affected to obtain relief if that rate proves confiscatory].) (FN7)

E.

As was said in Cotati Alliance for Better Housing v. City of Cotati, supra, *728. 148 Cal.App.3d at p. 296, 195 Cal.Rptr. 825, "the purpose of rent control is not to make the landlord a private guarantor of affordable housing for tenants, nor is it to bring about

such a degree of decreased maintenance and services as to diminish the quality of housing available. The purpose of rent control is to permit an efficient landlord to pay all actual and reasonable expenses and receive a fair profit while, at the same time, protecting the public interest in having affordable and properly maintained rental housing available to the citizens of the community." As applied, the City of Santa Monica's 12 percent cap does not meet these goals. Accordingly, we hold that Kavanau is entitled to the result which follows from the validly applied MNOI formula, without the 12 percent cap. (FN8)

DISPOSITION

The judgment is reversed and the matter is remanded to the trial court with directions to enter a new judgment in favor of Kavanau and to issue a writ of mandate commanding the Board to permit Kavanau to implement the balance remaining of the increases determined by the hearing examiner to be [19 Cal.App. 4th 737] appropriate under the MNOI, without any reduction under Regulation 4107(a). If questions arise concerning implementation of this opinion, they shall be resolved by the trial court following appropriate hearings. Kavanau is awarded his costs of appeal.

SPENCER, P.J., and MASTERSON, J., concur.

FN1. Under the MNOI formula (which is a return on investment standard), the landlord's 1978 earnings are presumptively a "fair return" and the regulation is designed to maintain this fair return in subsequent years by allowing rents to be raised based on increased operating expenses and inflation. (See Baker v. City of Santa Monica (1986) 181 Cal.App.3d 972, 976, fn. 4, 226 Cal.Rptr. 755; see also Fisher v. City of Berkeley (1984) 37 Cal.3d 644, 679-680, 209 Cal. Rptr. 682, 693 P.2d 261.) Rent control agencies are not constitutionally obliged to fix rents by any particular method but they are required to administer the selected formula in a manner which avoids confiscatory results. (Fisher v. City of Berkeley, supra, 37 Cal.3d at pp. 680-681, 209 Cal.Rptr. 682, 693 P.2d 261; see also Calfarm Ins. Co. v. Deukmejian (1989) 48 Cal.3d 805, 816, 258 Cal. Rptr. 161, 771 P.2d 1247 [the state and federal constitutions are concerned not so much with the way in which rates are set as with the result reached in the application of those rates].)

FN2. Kavanau actually spent an additional $18,400 on capital improvements during the same period but the Board's hearing examiner determined those expenditures were "unnecessary" to maintain the property and could not be used to calculate the allowable rent increase. This finding is not contested.

FN3. We are not asked on this appeal to decide whether the MNOI properly excludes from consideration a landlord's debt service. We note, however, that we can't accept the Board's overly broad assertion that this expense is properly excluded "because payments towards debt service build equity and therefore benefit the owner." "Debt service" includes interest, not just principal and, at a minimum, debt service is a factor which appears relevant to the determination whether, in fact, a landlord is receiving a fair return.

FN4. What this means is that Kavanau was denied the current use of the money the hearing examiner determined he was entitled to receive, and that he has permanently lost whatever interest or other income he could have earned with that money. It also means that any other increases which would automatically be justified over the next eight years (see, e.g., Regulation 1805(b) [which grants an automatic general adjustment pursuant to a specified formula] will be disallowed or at least indefinitely delayed because Kavanau will have already reached the 12 percent cap. (Birkenfeld v. City of Berkeley (1976) 17 Cal.3d 129, 169, 130 Cal.Rptr. 465, 550 P.2d 1001 ["'Property may be as effectively taken by long-continued and unreasonable delay in putting an end to confiscatory rates as by an express affirmance of them' "]; Cromwell Assocs. v. Newark (1985) 211 N.J.Super. 462, 511 A.2d 1273, 1276 [where there is no provision to factor in an increase lost because of a cap on rental increases, the cap "would cause a snowball effect of losses that might not be recouped"].)

FN5. As will appear, our review of Regulation 4107 is based on the current version, including subdivision (f). (Cf. Kash Enterprises, Inc. v. City of Los Angeles (1977) 19 Cal.3d 294, 306, fn. 6, 138 Cal. Rptr. 53, 562 P.2d 1302.)

FN6. The Board's interpretation of Regulation 4107(f) makes it unnecessary for us to determine whether any evidence Kavanau might have presented on his appeal to the Board could or should reasonably have been considered in deciding whether to waive the

12 percent cap. His building was not damaged by an earthquake. He just wanted to show that he would not be receiving a fair return on his investment if the amount the Board determined to be a fair return was reduced as required by the 12 percent cap. (See Fox v. San Francisco Residential Rent etc. Bd. (1985) 169 Cal.App.3d 651, 657, 215 Cal. Rptr. 565 [approving a cap on yearly increases because the regulation at issue permitted exceptions for "extraordinary circumstances" and empowered the hearing officer to consider all "relevant factors" in determining whether a rent increase in excess of the cap was justified].)

*728 FN7. It is not and could not be disputed that Kavanau could not obtain a fair return under the Board's approach. To the contrary, his deficit for the year in question would be $111,871--$98,099 of allowed operating expenses and capital improvements, plus $18,400 of expenses Kavanau incurred but the Board determined were "unnecessary," plus $44,000 in debt service, less $43,444 in existing rents, less the allowed increase of $5,184, equals $111,871. (See Cotati Alliance for Better Housing v. City of Cotati, supra, 148 Cal. App.3d at p. 293, 195 Cal.Rptr. 825 [inherent in the due process standard of "a just and reasonable return" is the assurance that an efficient landlord may recover all reasonable expenses actually incurred and, in addition, receive a fair profit or return on investment].) And while it is true that a deficit, standing alone, is not determinative of whether a landlord is earning a just and reasonable return, a deficit of this magnitude does not leave a lot of room for debate.

FN8. We do not express a view about what might happen if, in future cases, the Board broadens its interpretation of "extraordinary circumstances" under Regulation 4107(f).